THE FISCAL ROLE OF LOCAL GOVERNMENT IN DEVELOPING COUNTRIES: LESSONS FROM KENYA

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ABSTRACT

This thesis develops a basic framework for analyzing the fiscal role of local government in less-developed countries, and applies it in a comprehensive case study based on two years of fieldwork in the Republic of Kenya.

In recent years, there has been a growing interest in strengthening local government in developing countries for a variety of reasons. The public finance literature on the topic, however, remains very limited. Economic theories and models of local government have been formulated in the context of the developed countries. Although many of their basic principles are universally relevant, at least to some degree, numerous diverse, extreme, and unique circumstances limit the direct applicability of certain aspects of these theories to the developing countries. The framework developed here takes into account a wide variety of political, cultural, legal, constitutional, financial, and institutional constraints relevant in less-developed countries.

Most previous case studies of local government finance in developing countries have focused on particular aspects of the system or a few large cities--they have not been comprehensive and have largely ignored small and rural local authorities. In the study of Kenya, the fiscal role of small and large urban and rural local authorities is analyzed and evaluated, and an agenda for reforming the current system is outlined. Information and insights gained from the Kenya case study are used to clarify and highlight the unique factors that must be taken into account in analyzing the fiscal role of local government in developing countries.

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INTRODUCTION AND ACKNOWLEDGEMENTS

This thesis is based on research conducted in Kenya from May, 1986 through July, 1987. The conclusions and recommendations are based on the situation in Kenya during the early part of 1988. After the general elections held in late March 1988, a number of important institutional changes in the structure of Kenya's central government were announced. None of these changes had been implemented as this thesis was being finished, and it is likely to be some time before their effects can be analyzed; thus, most of these changes have not been explicitly reflected in the text of this thesis. The most important of the changes is that the former Ministry of Local Government has become the Ministry of Local Government and Physical Planning, a move that should ultimately strengthen the institution. In addition, the former Ministry of Works, Housing, and Physical Planning is now the Ministry of Public Works, and the former Ministry of Lands and Settlement is now the Ministry of Lands and Housing.

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CHAPTER 1

LOCAL GOVERNMENT IN DEVELOPING COUNTRIES

The purpose of this research is to develop a basic framework for identifying an appropriate fiscal role for local government in developing countries and to apply it to a single country. The framework will be used to conduct an exploratory and evaluative study of the fiscal role of local government in the Republic of Kenya.

The presumption underlying this study is that developing countries tend to underutilize local levels of government or to use them ineffectively.[1] However, there is a growing interest in developing or reviving local government in less-developed countries. In order to undertake this task effectively, there must be a reasonable methodology for analyzing the structure of the public sector in these countries, with particular emphasis on defining an appropriate fiscal role for local government.

A major problem in articulating such a methodology is that the context in which the local governments in developing countries operate differs very widely. These countries have very different histories, and there are extreme differences in political and economic systems, institutional

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[1] The factors underlying this presumption will be explored later.

organizations, cultural heritage, and constitutional and legal constraints on local government. This great diversity, which is documented in Chapter 2, makes the development of generalizable theories and models to analyze the problem virtually impossible; nevertheless, it is possible to identify important factors that need to be considered in defining an appropriate fiscal role for local government in developing countries.

Although the major focus of this research will be on a single country, the information and insights gained from this effort will aid in the development of a methodology and allow the formation of some generalizations about how to analyze the fiscal role of local government in developing countries. The analysis will be conducted primarily from a public finance point of view, but the exercise is by its nature an interdisciplinary one, which draws to some extent on literature in other fields.

Development Economics and Public Finance Background

Although there has been a great deal of research conducted on public finance and taxation in developing countries, very little attention has been paid to the fiscal role and finances of local government. Most of the research on this topic has been in the form of case studies or chapters in studies of national tax systems, usually conducted by national tax system study commissions or major international development agencies, such as the World Bank. This scarcity of research has undoubtedly occurred largely because of the small role that local government has traditionally played in most developing countries. Furthermore, traditional development strategies have tended to focus on central planning, large-scale industrialization, and spatial centralization to capture economies of scale and promote economic growth [Lewis (1954); Hirschman (1958); Brenner (1966); Alonso (1971); Richardson (1973); Todaro (1981); and, Wheaton (1981)]. To a great extent, these strategies require that public sector development policies be designed and administered at a central level and have generally ignored local government.

Recently, this emphasis on centralization in development has begun to change dramatically. Many newer development strategies have focused on decentralizing the public sector, slowing the growth of large urban areas, and regionalizing development [Mera (1972); Richardson (1977); Todaro (1981); Kelley and Williamson (1982); Cheema and Rondinelli (1983); and, Rondinelli (1984)]. Major international development agencies, such as the World Bank, the International Monetary Fund, and many bilateral aid agencies, have stressed policies of decentralization. Proponents of egalitarian development have stressed the greater equity inherent in decentralized development and the growth-stimulating effects of redistribution [Chenery (1974); Cline (1975); Mellor (1976);

N.L. Hicks (1979); Todaro (1981); and, Gillis, et. al. (1987)]. A number of analysts have suggested that the weakness of local institutions in developing countries severely constrains both economic growth and improvements in equity [Uphoff and Esman (1974); ILO (1974); and, Mawhood (1974)].

Although there are many forms of decentralization, it might be expected that strengthening local government would be one of the more obvious and important ones in many less-developed nations.[2] Nevertheless, the recent emphasis on decentralization in developing countries has not greatly stimulated the literature on the fiscal role of local government in the developing world. Only a few attempts to conceptualize the issues broadly and/or to compare local finance policies across a group of countries have been made. Some of this literature, e.g., U. Hicks (1961a, 1961b, 1978), predates the emphasis on decentralized development, and most of the rest of it focuses primarily on major urban areas [Bahl (1979, 1981); Linn (1981); Bahl and Miller (1982); Davey (1983); Cochrane (1983); Bahl, Holland and Linn

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[2] In fact, much of the emphasis on decentralization in developing countries has focused on working through local-level representatives/offices of central government ministries/agencies, a process known as deconcentration. In some cases this is appropriate, but in other cases, it is more appropriate to decentralize through local authorities, process known as devolution. The strong emphasis on deconcentration is, at least in part, nothing more than a manifestation of the central government fear of significant decentralization to be discussed later in this chapter.

(1983); Bahl and Linn (1983); Mawhood (1983); and, Bahl, Miner and Schroeder (1984)]. This research explicitly emphasizes the potential for decentralization of the public sector and improving the role and performance of the local government sector.

Most of the theoretical public finance work on local government's economic role has been developed in the context of industrialized countries [Tiebout (1956); and, Oates (1972)]. These theories are not directly transferable to the developing world because the history, development, context, and practice of local government in developing countries often differs greatly from the developed countries. Therefore, the analytical tools used to evaluate the fiscal role of local government in the developed countries require some modification for application to a developing country. This will be discussed further in Chapter 3.

Underutilization of Local Government in Developing Countries

In industrialized nations around the world, local governments often have an important role to play in the national political and economic scene. In Organization for Economic Cooperation and Development (OECD) countries, for example, local government accounts, on average, for 11 percent of total public sector employment. In a number of the member countries, the figure runs as high as 20 to 25 percent. By contrast, the governments of developing countries are highly centralized. The average share of public sector employment accounted for by local government in these countries averages 4.5 percent, ranging from 2.5 percent in Africa to 8 percent in Asia [Cochrane (1983), p.1].

There are a number of reasons why local government has not played a major role in most developing countries. First, the type of local government introduced by colonial powers in developing countries is often very alien and lacks legitimacy among the native people.[3] Even in areas where traditional native chiefs or councils have long existed, these institutions have often gained their legitimacy by traditional succession or custom, e.g., the automatic appointment of elders to a governing council. The idea of a council elected on other lines may take time to be fully accepted, particularly in places where local tradition is important to the people. In addition, in areas where the cash economy is a relatively new phenomenon, people are used to living at a subsistence level and being largely self-sufficient. They are not accustomed to dependency on modern administration and services provided by the government, nor are they accustomed to paying for these services.

Another important reason for the underutilization of local government in developing countries is that, even in

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[3] For a more detailed discussion of this issue, see Mawhood (1987).

some areas where local government was introduced early in colonial times, local institutions were never properly developed. Colonial authorities may not have felt a need to involve natives in self-government in a meaningful way until great pressure was put on them to do so just prior to independence. Local government institutions in many countries were designed for the settlers, not the natives. Many of the settlers have returned to their countries of origin in the post-independence years, leaving the natives with an institutional framework that was not designed with their culture and needs in mind. Even in places where strong local government was institutionalized for the natives, its functions were often administrative and regulatory, and they had little to do with self-determination and economic development.

As noted earlier, for most of the early years of development economics, developing countries were advised that they could be more effective by centralizing control over the economy. Development policies tended to focus on central planning, industrialization, and centralization of development in major cities, despite the fact that a majority of the population were often engaged in agriculture in rural areas and nationals of the country lacked the capital to initiate and sustain large-scale investments. In addition, important economic functions traditionally cited as primary government responsibilities in the developing countries, such as macroeconomic stabilization and international trade management, must be undertaken by central governments. For all of these reasons, the principal public sector focus for economic policy has been on the central government, and local authorities have been largely neglected.

In many developing countries, there is a lack of managerial and technical expertise to staff local governments effectively. Because of this lack of skilled personnel, it has not been possible to develop local government institutions and an effective working relationship between the central and local governments. Because the pool of human resources is so limited and training and educational facilities so scarce, the central government may fear losing some of its essential qualified people to decentralized levels of government if the latter are strengthened. Furthermore, the central government financial resources to develop and aid decentralized institutions are simply not available in many developing countries.

Perhaps the most important reason why local governments have been neglected in developing countries is that there exist many strong central governments that do not wish to share their power [Rondinelli (1983); and, Cochrane (1983)]. Often in the name of national unity, central governments in developing countries have weakened local government institutions set up by the colonial administrations and refused to grant local governments significant powers. Many governments in developing countries are somewhat unstable and insecure, and they feel the need to consolidate control in order to introduce an element of stability and protect the interests of their leadership. In many developing countries, the income distribution is very skewed. It is concentrated among a powerful modern elite who see it as in their best interests to keep control in their own hands and therefore to prevent any meaningful decentralization of power and redistribution of wealth. In some cases, the ruling elite are dominated by particular tribal or ethnic groups who are reluctant to share power with rival groups.

The political tendency towards centralization in many developing countries manifests itself in a wide variety of constraints on the development of local government, which the central government can use as an excuse for not doing more to strengthen local authorities. Many of these constraints are constitutional or legal in nature. In some countries, for example, local authorities can do little without lengthy review and approval by a central government ministry. In others, there are severe constitutional or legal limits on the revenue-raising and service-provision powers of local authorities. The result of these types of restrictions is that local governments cannot operate efficiently and effectively. Other constraints are more explicitly political. In some countries, a few select local governments may benefit from central government technical and political figures in the central government who come from the regions in which the favored local authorities are located. Other local authorities may be left to fend for themselves under more difficult conditions.

Some types of constraints on the functioning of local authorities are more local in nature. Even in some developing countries where local governments are properly empowered, they may not be able to operate effectively because of local problems. For example, property and business-based taxes may be greatly underutilized in some local authorities because the local government is to a great extent under the control of major landowners and businessmen who do not see such taxes in their best interests. This can greatly hold back the development and performance of local authorities. In addition, local tribal systems might justifiably undermine the local political process because their interests and traditional institutions were not sufficiently taken into account when the local government system was set up. Particular local authorities might also be subject to some of the other types of constraints discussed earlier, such as a lack of resources and trained personnel, even if the country as a whole is not as seriously affected.

The Case for Local Government in Developing Countries

Despite the obstacles to effective local government institutions in developing countries, a strong case can be made for defining a more substantial role for them. The more prominent role of local government in developed countries suggests that local authorities may have an important role to play in the management of development. In a recent World Bank publication, Cochrane has gone so far as to state that an effective public sector in a modern developing country "depends on the ability of the central government to harness the resources of lower levels of government" [Cochrane (1983), p.1].

Local governments are often the institutional overseers of the population centers in which most industrial and specialized nonindustrial economic activities are based. The jurisdictions that they govern may generate the primary demand for the agricultural production of the surrounding territory, and they are the communications and transport centers for their local region. These centers provide the input-output linkages for rural production and are the concentration points for marketing activities. Given limited central government resources, the effectiveness of local authorities in providing infrastructure and an atmosphere conducive to economic activity can have an important influence on the success of the local economy and its potential for future development [Rondinelli (1982); Little (1984); and, Belsky and Karaska (1984)].

The role of local authorities in the local economy also means that they can play an important role in supporting and/or implementing macroeconomic and national development policies. Where there is limited central government presence, local authorities are in a good position to mobilize support for national development policies by their actions and by making these policies more widely known at the local level [Rondinelli (1978 and 1981)]. This is particularly important in countries that are large and/or in which it is difficult to travel to remote areas because of poor access roads and harsh climatic conditions. In such cases, it may not be practical for the central government to keep in good contact and work effectively with some areas of the country. From a purely managerial standpoint, the administration of development policies in widely scattered locations throughout an entire country can be extremely difficult. In short, under certain conditions common in developing countries, local governments will be able to mobilize financial, political, and social resources and manage some aspects of economic development more effectively and efficiently than the central government. They will also be better able to disseminate information about and implement national development policies.

In some developing countries, local authorities may be able to provide certain kinds of vital services that it is not practical or possible for the private sector or the central government to provide. In some cases, for example, particularly in rural areas, the private sector cannot afford to provide facilities for local producers to market their goods. Although it might be possible for the central government to finance such facilities, often through donor funds, it may not be practical for the central government to staff and maintain them due to limited resources. In such cases, it may be appropriate for local authorities to assume responsibility.

Local authorities can also have an impact on population policies and settlement patterns in that their effective development and management can play a role in helping to curtail the excessive growth of population and economic pressure in the primary urban centers [Evans (1986)]. The process of continuing urbanization in smaller local authorities creates new wealth through increases in economic activity, income, and land values, drawing still more people and employment to these areas.

More intensive development of smaller local areas also has the potential for longer-term equity gains. A variety of recent research cited earlier has suggested that decentralized development has a tendency to lead to a more equal distribution of income. Other things being equal, such redistribution has the potential to generate an increase in income and further economic growth through the increased multiplier effects that result from higher marginal propensities to consume among lower-income people.

Another important reason for greater utilization of local government in developing countries is that there is little evidence that more centralized service provision in developing countries is any more efficient than local service provision. If fact, economists would argue that, for many services, just the opposite is true. In the absence of economies of scale, externalities, and uniform demand for a service over a large area, it is more efficient to assign service provision to decentralized levels of government. Decentralization allows for better government adaptation to dissimilar circumstances and preferences across local areas. This issue of assignment of public sector functions to local authorities is a key issue in this thesis and will be dealt with extensively in Chapter 3.

Perhaps the most important reason for strengthening local authorities is that they are the institutions that are closest to the people at a grassroots level. Local government has great potential to increase the level of local participation in the development process and, by definition, to increase the degree of self-government. Williams (1981) has suggested that successful development strategies require greater participation of their intended beneficiaries, from the planning to the evaluation stage. Some analysts have argued that greater equity in the allocation of government resources will be realized when representatives of a wide variety of political, religious, ethnic, and social groups participate in decision-making [Montgomery (1972); Uphoff and Esman (1974); and Esman and Montgomery (1982)]. If local government is given a greater role, it may be more possible to retain local culture, values, and customs, which are extremely important to the people in some countries of the developing world. Finally, when local people have problems and need help, they often come to local government officials first. Because local authorities are staffed by people familiar with local conditions, they have a greater potential than does the central government to respond effectively to many local needs.

Despite the above arguments made in favor of stronger local authorities in many developing countries, it is important to recognize that decentralization and an enhanced role for local authorities are not desirable and necessary in all developing countries. Some countries are geographically small and/or ethnically and economically homogeneous. In such cases, a well-organized central government may be adequate to ascertain the needs and desires of the people and to formulate and implement effective development policies.

Even in developing countries where a case can be made for strong local government, the importance of central government coordination of development activities must be acknowledged. Decentralization can go too far and lead to the development of local authorities who work against the best interests of the country as a whole. Local authorities should be responsive to national needs and be willing to explain and support national policies in their jurisdictions. Of course, local authorities have their own development responsibilities and priorities, but they should not be in conflict with overall national development objectives, as articulated through a broad-based and democratic political process.

Renewed Interest in Local Government in Developing Countries

In recent years, there has been a pronounced interest in developing or reviving local government in less-developed countries. This interest has come from the governments of developing countries, academics, and international development organizations. Part of the explanation for this upsurge in interest is a realization of the potentially productive role for local government described above. It was, however, significant changes in economic and political situations that actually triggered concrete action.

Throughout much of the 1970s and 1980s, the world economy has been confronted with a variety of problems particularly affecting the developing countries, which have been less able to deal with them than the developed countries. At various times during these years, there have been periods of extreme inflation, collapses in the prices of important agricultural and natural resource commodities on which developing countries rely for foreign exchange, serious droughts in parts of Africa and Latin America, and an extended period of worldwide recession. During the same period, many developing countries saw their trade policies, such as import substitution, fail to a great extent. There was slower economic growth than there had been a decade earlier, and in some countries population growth was exploding at a tremendous rate. The combined effect of these and other trends was tighter government budgets during a period of time when demand for government services was growing rapidly.

Because of their economic problems, many developing countries began to generate large government budget deficits, which were financed primarily by external borrowing. Over time, interest payments began using up higher and higher percentages of government resources, and the vicious cycle of borrowing and overspending escalated. It is now very clear that many central governments in developing countries have been living far beyond their means for years, and that they were actually encouraged to do so by the lending policies of the developed nations. At the same time, the labor force has been growing rapidly as population grows, while actual employment opportunities are increasing at a slower rate.

The implication of these developments is that governments in developing countries cannot continue to expand at their rapid historical rates and must try to focus on self-financing and more productive public investments. In some countries, this situation is likely to necessitate temporarily placing less emphasis on social services, such as health and education, and more emphasis on basic infrastructure services, such as water, roads, and electricity, which have the potential to stimulate private sector investment. It also suggests that the central government may have to reduce its role in managing certain development policies and rely more on local governments, which are often underutilized and may have tremendous untapped revenue potential. In some developing countries, local authorities are the only decentralized institutions with adequate administrative capacity and legal or constitutional powers for raising revenue and providing public services.

The new focus on a greater fiscal role for local government has been advanced greatly by major international development agencies, such as the World Bank and the International Monetary Fund. These institutions have conducted a variety of research on strengthening local government and have implemented a number of programs requiring their participation. Local government has also received a boost from revised aid guidelines and policies of a number of major bilateral aid agencies. In the wake of the economic problems of the 1970s and 1980s, conservative movements and governments have become more influential and moved into power in many developed countries. One result has been that the bilateral aid agencies have tried to redefine the types of projects that they will support with grants and loans. There is less emphasis on financing central government programs because of a bias against central planning and control, and more emphasis on the market and decentralized institution-building that supports the growth of the private sector. Such policies will often be administered through decentralized agencies of the central government and local authorities. The additional burdens on local authorities in many countries have led to calls for strengthening them.

Reliance on local government may further increase in coming years as the governments of some developed countries continue to cut back their own scale of operations. Economic aid to developing countries is likely to be one of the first budget lines to receive cuts in conservative political and difficult economic times, and the developing countries may have to learn to be less and less dependent on foreign aid. The worldwide stock market crash of October 1987 and potential forthcoming repercussions may force additional major economic policy adjustments that a number of developed nations have been avoiding for some time, further affecting the developing countries. Development aid is certain to be affected by the efforts of the United States to reduce the federal budget deficit in the wake of the crash. If the U.S.

economy enters a recessionary period and other major economies follow, a further deterioration in development aid is likely to result.

Cutbacks may occur not only in aid to the governments of developing countries, but also in industrialized country funding for certain types of non-governmental organizations (NGOs) and charities. In some areas of the developing world, these organizations provide a substantial level of important services at the community level. If these services are seriously reduced, local governments and indigenous self-help groups might be called on to keep particular programmes and services afloat.

Grassroots political factors have also certainly had an impact on the new emphasis on local government. As people become more educated and more informed through improved communications, they often want to have a greater say in the matters that affect their daily lives. There is greater awareness of the waste and corruption in many central government bureaucracies, and people desire to bring the control of government functions closer to themselves. In a number of developing countries, there has been a movement towards greater democracy as military regimes are forced to relinquish power and institute democratic reforms.[4] This

[4] Of course, the deteriorating economic conditions in developing countries discussed above are a primary factor in the toppling of military regimes, but greater political awareness and better political organization also have a role to play.

sets an example for other countries and emboldens people to push for still further changes. Political pressure from below and from the international community forces central governments in developing countries to continue the process of reform. In some developing countries, part of this reform has included efforts to decentralize.

The process of decentralization in developing countries may be, at least in some cases, encouraged by cultural factors. Peoples of the developing world have begun to revive a positive opinion of their own traditional cultures in recent years. There is, of course, still a great deal of interest in the western cultures and values brought to developing countries during the colonial era and evident in modern mass media. Developing peoples, however, are also nurturing a new pride in their own heritage, which may in the past have been something that native people who were exposed to western culture tried to hide.

In certain traditional cultures, there is a history of community self-government and an emphasis on collective, rather than individual, values. Given the resurgence of cultural awareness, people may be more inclined to want to participate in decentralized institutions and processes, which give them a sense of identity and self-determination. The quality of government and public services may improve greatly from this cultural rebirth in some developing countries.

Objective of the Thesis

There has been a renewed interest in strengthening local governments in developing nations in recent years, but little new literature has been generated on defining an appropriate fiscal role for local governments in these countries. The primary purpose of this study is to develop some concrete insights into the problems of designing an effective public sector in developing countries with an appropriate role for local authorities. The first objective is to understand more fully the existing problems in local government organization and administration for a single case study country. This requires trying to demonstrate what an appropriate role for local government might be, and documenting how and why the system falls short of the normative target as well as what the consequences of these deficiencies are.

The second objective is to get a clearer sense of the types of problems and constraints that seem to be responsible for these deficiencies, to determine which of the problems can be eliminated or alleviated, and to identify the types of corrective policies that might be employed. Going through this process for one country will help to clarify the major issues and problems involved in analyzing decentralization and local government in the developing world. The process will lead to a clarification of the analytical framework as well as some useful generalizations about the analysis of the fiscal role of local government in developing countries.

This chapter has briefly reviewed the historical role of local authorities in developing countries and suggested some reasons for their underutilization. It has also documented the reasons for the renewed interest in local government in the developing world, as well as some of the problems and issues in analyzing local government in developing countries.

Chapter 2 will explore the tremendous variation in the organization and practice of local government in developing countries. There will be a discussion of general types of systems, as well as eight brief case studies documenting the diversity of local government systems in the developing world. It is important to take this diversity into account in analyzing the role of local government in the less-developed countries.

Chapter 3 will outline a basic framework for the central task of this thesis: analyzing an appropriate fiscal role for local governments in developing countries. Economic theories of local government in developed countries will be reviewed, and their relevance for developing countries assessed.

Chapter 4 will explore in some detail the history, development, and current structure of local government in the main case study country, Kenya. This exercise will demonstrate how political and cultural factors, as well as historical accident, affect the nature of the local government system that develops in a given country. These factors also provide a background to refer to in the following chapters, in which the current system of local government in Kenya is evaluated.

Chapters 5 and 6 will use the framework developed in Chapter 3 and the background information presented in Chapter 4 to analyze and evaluate the current system of local government in Kenya. This will include a discussion of the various non-economic factors that have influenced the development of local government in this country and may still, to some extent, define the boundaries within which the system of local government must lie.

On the basis of the evaluation in Chapters 5 and 6, Chapter 7 will outline a set of recommendations for reforming the fiscal role of local government in Kenya.

Finally, Chapter 8 will summarize the major findings of the thesis and discuss the lessons learned from the Kenya case study regarding the factors and processes that are important in defining a fiscal role for local government in developing countries.

CHAPTER 2

DIVERSITY OF LOCAL GOVERNMENT SYSTEMS IN DEVELOPING COUNTRIES

There has long been pessimism about the possibilities for developing democratic local government institutions in the less-developed countries. With few exceptions, observers and analysts of local government in developing countries felt that the strong centralization existing in many places would be difficult or impossible to overcome. Walter Oyugi, Professor of Government at the University of Nairobi and an expert on local government in developing countries, has summed up the situation in this way:

> In the underdeveloped countries the grassroots democracy motive is rarely found. Noble as the ideal of political development is, it does not at the moment seem to concern the ruling cadres. Their concern in this sphere seems to be the attainment of political conformity and central government hegemony over the local communities and institutions. Hence it has become a common observation that governments in most of the underdeveloped countries are predisposed to controlling the behavior of their local citizenry and, therefore, cannot be expected to contradict their prime objectives by offering village democracy to the people [Oyugi (1973), p. 56].

During the past ten years or so, there has been some cause for greater optimism that decentralization will succeed, as discussed in the previous chapter. How it will proceed and the forms it will take are likely to vary greatly, largely because developing countries are such a heterogeneous group.

There is a great diversity in the types of local government systems that operate in developing countries. As noted in

Chapter 1, this is important because the tremendous variations in context make it very difficult to analyze local government in developing countries with the types of generalizable theories and models normally used by economists. There are great differences across countries in types of political and economic systems, institutional organizations, and cultural, social, and historical influences, all of which can have a great effect on how the system of local government has evolved and operates. These factors also strongly affect the approach that needs to be taken when these systems are being analyzed.

The purpose of this chapter is to sketch a brief outline of some of the different types of local government systems operating in the developing world and to examine the fiscal role of local authorities in these systems. First, a general overview of various types of systems is presented. This is followed by brief descriptions of the local government system in a small sample of diverse developing countries. The latter exercise is intended to give some concrete examples of the diversity existing among these systems, which has an adverse impact on the possibilities of generalizing about local government in the developing world. An understanding of the differences among the systems will be useful in the next chapter, where a framework for analyzing the fiscal role of local government in developing countries is developed.

Overview of the Range of Functions and Powers of Local Government in Developing Countries

Systems of government in the developing world are basically of two types: unitary systems and federal systems. By far the overwhelming majority of developing countries are unitary states in which the source of the state's power is the central government. To the extent that local government exists, it is a creation of the central government. Federal states are ones in which the federal (central) government exists by virtue of a union of decentralized units, which join together and agree to surrender certain powers to the central government.[1]

Unitary governments permit the existence of a wide variety of decentralization. In some unitary states, there are no local governments, although there may be decentralized administrative units of the central government. Under the field or local administration system, local governments operate largely as extensions of the state bureaucracy with few autonomous powers. This is the system that was imposed by the French in most of their former colonies, e.g., Cote d'Ivoire, Mali, the People's Republic of Benin (formerly Dahomey), Tunisia, etc. In extreme cases, the central government may even appoint the members of local government councils rather than permitting their election by popular

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[1] For a good discussion of these systems and the logic behind them, see Smith (1985).

vote.

In former British colonies in the developing world, a genuine system of semi-autonomous local government was normally established. The local authorities are legal entities, which can sue and be sued as well as enter into independent contracts. This type of system, which exists, for example, in Kenya, Zimbabwe, and Uganda, often retains a significant degree of central control, but local authorities are usually governed by locally elected councils which have some degree of fiscal autonomy.

In either the local administration or local government system, there are sometimes several tiers of decentralized government units, while in a federal system this is always true. For example, there may be states, provinces, regions, or districts at an intermediate level, while at the most decentralized level there would be local authorities, such as municipalities, towns, and urban centers. Sometimes none of the decentralized levels of government have much autonomy, e.g., the Sudan and Thailand. In some cases, e.g., Nigeria, Papua New Guinea, and Mexico, the intermediate levels are more powerful than the most decentralized levels, while in other cases, e.g., Colombia and Venezuela, the intermediate levels have few responsibilities and powers compared with the local levels.

There are also various kinds of autonomy displayed in local government systems. First, there is the issue of political autonomy. This has to do with whether or not local government councils are elected by the people or appointed by the central government, as well as how independent they are from central government politics and policies. There is also the issue of fiscal autonomy, which relates to the degree of independence in revenue-raising and spending decisions. In some cases, e.g., the Sudan, local governments have little control over how they raise and spend their revenue. In other cases, e.g., Papua New Guinea, local authorities may have significant discretion over spending questions but be largely or fully dependent on the central government for revenue. In still other cases, e.g., Indonesia, local authorities may have access to a wide variety of income sources but substantially less than full discretion about how the funds are spent. Finally, there are at least a few developing countries, e.g., India, where local authorities have a fair degree of both revenue-raising and spending autonomy.

The type of government system that exists in a particular developing country depends on a variety of factors. Principal among these are the indigenous culture and customs and the legacy of the colonial power in the country. Each country has its own history, during the course of which a system of government evolved to suit the needs of the country's leadership and/or people.

In many developing countries, the system of local government is still evolving. In others, lack of stable political institutions means that the degree of decentralization is not constant. In many countries, there seem to be ebbs and flows of enthusiasm for decentralization. Mawhood (1987, p. 22), a seasoned observer of local government in developing countries, explains this erratic cyclical pattern as follows: "Perhaps we can conclude that successful decentralization occurs when the political weather is good (that is, the regime is strong and unchallenged) but the economic weather is bad (it suffers a painful shortage of resources)." This suggests that, at least in some developing countries, the process of establishing strong decentralized institutions has been and will continue to be slow and difficult.[2]

The reality is that the vast majority of government systems in the developing countries tend to be highly centralized. Although local institutions may account for a significant percentage of public sector expenditures, they rarely have a substantial degree of both political and fiscal autonomy. Allen (1987) argues that true community-

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[2] There are cycles in levels of decentralization and the nature of intergovernmental relations in some developed countries as well. In the 1960s and 1970s, for example, state and local governments in the United States were increasing their public expenditure role but decreasing in their level of revenue self-sufficiency as federal government grant programs increased. In the Reagan years, there has been a clear movement to reduce central government support of state and local government at the same time that taxpayers are taking a stand against increases in state and local taxes.

based local government exists only in a handful of countries, e.g., Tanzania, Cuba, South Korea, and India, usually for ideological reasons. Even in such cases, however, there is often a high degree of dependence on the central government.

In spite of the instability and great diversity of local government systems in developing countries, it is possible to identify a few general trends in the development of local government which exist in different parts of the developing world.[3] Local governments in most Asian countries are bureaucratic instruments of the central government rather than agents of local participation. In many parts of Asia, there is a long history of empires and traditional central rule. Many Asian cultures also emphasize social harmony, order, and cohesion. There is a strong sense of duty and obedience in these societies, and it blends very well with centralization. There are, however, some exceptions and qualifications to the Asian rule of centralization. Although the public sector in China is quite centralized, for example, local governments have significant autonomy over certain functions. In some of the former British colonies on the Indian subcontinent, there is a highly developed system of local government remaining from the colonial era.

In most of Africa, centralization is also the norm, largely because of the legacy of colonial powers on this continent. Highly centralized government systems exist in

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[3] For a more detailed discussion, see Mawhood (1987).

most of the francophone countries in west, central, and north Africa, although some of these countries are making attempts to decentralize. Anglophone countries in east, southern, and west Africa generally have more autonomous local governments, but strong central governments still tend to dominate the public sector. Africa is an interesting case because many of the African cultures are very well-suited to local government. Many Africans are accustomed to small-scale tribal government and highly local decision-making processes. Possibly because of this, there are strong village self-help movements in Africa, even in some areas where modern local government is fairly limited.

Latin America government systems are more decentralized than their counterparts in Asia and Africa, but there is still not a great deal of local government autonomy in most countries. The majority of Latin American countries gained their independence from colonial powers much earlier than the countries of Asia and Africa, and this has given them more time to develop decentralized institutions. In addition, some of the larger Latin American countries developed decentralized government in major regional cities far away from national capitals during colonial times, and the tradition has continued [Mawhood (1987), p.18]. Even in the federal systems such as Argentina, Brazil, and Mexico, however, much of the institutional development has been at the state level rather than the local level. Thus, the states and regions often play a very significant fiscal role, while the role of the local governments is much more limited.

Comprehensive comparative data on the role of decentralized government across developing countries is not currently available, but there are a few dated studies that provide some useful information. Table 2.1 gives information on the percentage of 1968 total government spending accounted for by subnational governments in 44 developing countries. Although the data are old, they give an indication of the enormous variation in the size of the decentralized public sector in developing countries. Furthermore, they basically confirm the geographic generalizations made above about the role of decentralized government in different areas of the developing world. However, two points of caution are in order. First, having a high percentage of expenditure accounted for by decentralized government does not necessarily mean that local governments have a significant role to play, nor does it mean that the decentralized levels of government are necessarily autonomous in their revenue-raising powers and expenditure functions. Second, the data should be used for very rough comparative and illustrative purposes only. Some significant changes have certainly occurred in some of these countries since 1968. For example, the importance of the Kenyan decentralized government sector has declined dramatically since 1968 because some major service responsibilities and revenue

TABLE 2.1

SUBNATIONAL GOVERNMENT PERCENTAGE SHARE IN TOTAL GOVERNMENT CURRENT EXPENDITURE IN DEVELOPING COUNTRIES, 1968

Countries with Large Subnational Share	
Brazil	65.8
Colombia	54.2
Chile (1967)	52.7
India	52.3
Mexico	47.5
Pakistan	44.5
Uruguay	44.4
Ecuador	41.4
Venezuela	41.2
South Africa	40.1
Cameroon	40.0
El Salvador	39.2
Çosta Rica	37.5
Bolivia	37.2
Median	42.9
Mean	45.6

Countries with Medium Subnational Share	
Korea	28.9
Nicaragua	27.7
Nigeria (1969)	27.4
Malagasy	25.8
Ireland	21.5
Portugal	21.5
Botswana	20.5
Phillipines	20.4
Honduras	20.1
Kenya	18.9
Trinidad	18.3
Algeria	14.7
Guatemala	13.7
Turkey	10.9
Median	20.5
Mean	20.7

Countries with Small Subnational Share	
Malaysia	9.3
Rhodesia*	8.9
Panama	8.8
Tunisia	8.2
Senegal	7.8
Sierra Leone	6.3
Fiji	6.2
Thailand	5.7
Jamaica	5.6
Mauritius	5.5
Chad	5.3
Peru	3.8
Zambia	1.8
Swaziland	1.3
Lesotho	1.2
Ceylon**	0.1
Median	5.7
Mean	5.4

SOURCE: Woo Sik Kee, "Fiscal Decentralization and Economic Development" (Washington, DC: The World Bank, 1976), mimeo as cited in R. Bahl, Urban Government Financial Structure and Management in Developing Countries, (Syracuse, NY: Metropolitan Studies Program, Syracuse University, December 1982), p. 30.

*Zimbabwe

**Sri Lanka

sources were transferred to the central government in 1970.

Table 2.2 presents information on the percentage of local government expenditure financed from central government transfers in selected cities in a sample of developing countries. Again the data are old, mostly from the early and mid-seventies, and for this reason they should be interpreted with caution. However, they do illustrate the large variations across developing countries in the degree of local authority dependence on central government. Furthermore, the data show that there are extreme variations within particular developing countries in the degree to which central governments fund local government services in different local authorities.

Variations in Local Government in Developing Countries: Selected Brief Case Studies

In order to illustrate the degree of diversity in local government systems in developing countries, it is useful to give some concrete examples of different types of systems. This section presents very brief case studies of local government systems in eight developing countries, including: Brazil, Nigeria, Bangladesh, the Sudan, Papua New Guinea, Zimbabwe, Botswana, and Peru. These countries were selected so as to represent the spectrum of government organization, from a federal system to a highly centralized unitary state. They also illustrate a spectrum of responsibilities, from a

TABLE 2.2

PERCENTAGE OF LOCAL GOVERNMENT EXPENDITURE FINANCED FROM CENTRAL GOVERNMENT TRANSFERS (GRANTS AND SHARED TAXES) IN SELECTED CITIES IN DEVELOPING COUNTRIES

City	Year	Percent Central Transfers
Tunis (Tunisia)	1972	0.7
Bombay (India)	1970/71	1.0
Rio de Janiera (Brazil)*	1967	1.7
Francistown (Botswana)	1972	1.9
Kitwe (Zambia)	1975	2.2
Karachi (Pakistan)	1974/75	2.8
Cali (Colombia)	1974	2.8
Amedabab (India)	1970/71	4.2
Lusaka (Zambia)	1972	6.0
Mexico City (Mexico)	1968	8.9
La Paz (Bolivia)	1975	9.0
Valencia (Venezuela)	1968	9.2
Lumbumbashi (Zaire)	1972	9.5
Cartagena (Colombia)	1972	12.8
Bogota (Colombia)	1972	14.0
Seoul (Korea)	1971	15.8
Calcutta (India)	1974/75	19.5
Jakarta (Indonesia)	1972/73	21.1
Madras (India)	1975/76	25.1
Mbuji-Mayi (Zaire)	1971	29.8
Manila (Phillipines)**	1970	30.0
Bukaru (Zaire)	1971	30.1
Tehran (Iran)	1974	45.2
Kingston (Jamaica)	1971/72	67.2
Kinshasa (Zaire)	1971	73.1
Median		9.5
Mean		17.7

*Due to the exclusion of autonomous agencies which raise self-financing service revenues, the importance of central transfers is probably overstated.

**Total revenues are used as the base rather than total expenditures.

SOURCE: Johannes Linn, "Urban Finances in Developing Countries," in Urban Government Finance: Emerging Trends, edited by Roy Bahl in Urban Affairs Annual Reviews, Vol. 20 (Beverly Hills, CA: Sage Publications, 1981), pp. 258-259.

fairly high degree of financial self-sufficiency and decision-making autonomy to a low degree of both.

It is important to note that there is not a great deal of information available about local governments in developing countries, and much of what can be found is not very current. The brief cases presented here are extracted from fairly recent reports, articles, and/or interviews. The level of detail differs across cases because the quantity and quality of information available from the sources consulted for the case material varies greatly.

Brazil: A Strong Case of Federalism[4]

Brazil has one of the few federal systems in the developing world and one of the most developed systems of decentralized government. Since the last century, the Brazilian system of government has changed a number of times, alternating between various forms of federalism and unitary government. The current federal system is well suited for Brazil, which is one of the largest developing countries in the world. The country is divided into 23 states and about 4,000 local authorities (municipios).

All levels of government in Brazil have significant service responsibilities and revenue-raising powers. In 1978, the federal (central) government accounted for 72.6

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[4] The information on Brazil is from Mahar and Dillinger (1983).

percent of public sector current expenditures, 46.1 percent of public sector capital outlays, and 67.0 percent of total public sector spending. State governments made 24.6 percent of public expenditure current expenditures, 43.7 percent of public sector capital outlays, and 28.7 percent of total public sector spending. Local authorities, despite their number, had a much smaller role to play. In the same year, they accounted for only 2.8 percent of public sector current expenditures, 10.2 percent of public sector capital outlays, and 4.4 percent of total public sector spending. Thus, decentralized government in Brazil has a large fiscal role to play, but primarily at the state, rather than the local, level.

The service responsibilities of different levels of government are not very clearly specified, with the exception of obvious central government functions, such as defense. The Constitution allows the states to engage in any activities not specifically prohibited in its provisions. The local authorities are merely assigned responsibility for "local public services", without any definition of exactly what these are. These ambiguities have led to joint provision of many services across all levels of government. The states and local governments combined accounted in 1975 for a significant percentage of public expenditures (after transfers) in the following categories: housing and urban services, 99 percent; education, 74 percent overall, 98 percent primary; and, health and sanitation, 47 percent.

There is a great heterogeneity among Brazilian states and local authorities, but they, by and large, have access to good sources of revenue. The main source of state revenue is a modified value-added tax, which accounted for 59.2 percent of total state revenue in 1978. Local authorities rely heavily on a municipal service tax and property taxation, which together yielded about 33 percent of local income in the same year.

States are to a great extent self-sufficient, receiving only 19.6 percent of their revenue from federal government transfers. Local authorities were much more dependent on the federal government, with 39.7 percent of their total income coming from central sources. Only a small percentage of federal transfers to state and local governments are programme grants from general funds. Brazil has a revenue-sharing scheme in which percentages of central government taxes, including the income tax, the manufacturers' sales tax, the fuel tax, the vehicle registration tax, and the electricity tax, go to both state and local governments, and these tax shares represent the bulk of the transfers.

Both state and local governments clearly have some significant fiscal roles and powers in Brazil. However, there are still a number of areas in which the central government has a great deal of control over decentralized governments. For example, the freedom of the states to levy the value-added tax, by far their most important source of revenue, is controlled by the federal government. The latter has the authority to determine both the tax base and the tax rates. The federal government has similar powers over the municipal service tax, but not over the municipal property tax.

Nigeria: Strong States in a Quasi-Federal System[5]

Like most former British colonies, Nigeria has a long history of local government. It is unusual, however, in that it also has a very powerful system of state government. The Nigerian Constitution recognizes federal, state, and local governments. It is not a true federal system because the states are a creation of the central government, but it does operate like a federal system in that the states have substantial autonomous powers with which the central government cannot interfere.

Local governments have not been strong historically in Nigeria. It is interesting that the local government reform movement arose during an era of military control. In 1976, the military government issued a set of guidelines designed to strengthen local government. The explanation given for this move was that there was a need to institute participatory democracy as a prelude to the impending return

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[5] The information on Nigeria comes from: Gboyega (1983); Cochrane (1983); Rondinelli, et. al. (1983); and, Nooi (1987).

to civilian rule.

In the 1976 guidelines, Nigeria devolved a wide range of functions to the local governments. These included: maintenance of law and order; construction and maintenance of secondary public roads and bridges; formulation and implementation of rural development schemes; agricultural development; and, provision of local services, such as health, housing, and water. The Nigerian local governments have access to a variety of revenue sources, including a community tax, property rates, license fees, and service charges.

Local government councils are supposed to have a fair degree of local representation. Some local council members are elected directly, but some are appointed by the state governors. The states have a great degree of control over the local councils. Local functions and revenue sources are heavily regulated by the state governments. Local governments are also heavily dependent on the state and federal governments for revenue. The higher levels of government are required to make statutory grants to local authorities. The federal government must provide 5 percent of its retained revenue through the states, while state governments must provide 10 percent of their own-source revenues to the local authorities in their jurisdictions.

The strong system of local government proposed by the mid-1970s military government has never materialized in

Nigeria. After the country temporarily returned to civilian rule in 1979, elections were held at the federal and state level, but economic and political factors did not favor strengthening local government. On the economic side, drastic declines in oil revenue meant that the resources to implement the decentralization programme were not there. On the political side, the states were very successful in blocking the implementation of the decentralization process. The state governments, by and large, did not share in the central government's enthusiasm for strengthening local authorities. State governors began appointing their strong supporters to local government councils and keeping tight control over local authority actions. There was little that the central government could do to force local authority reform because the states have the ultimate powers over local government in Nigeria. State governors may order the dissolution of any local government council in their jurisdictions at any time.

Today, many of the more than 300 local authorities in Nigeria basically operate as appendages of the state governments and without the full state and federal aid revenue that is due to them. In 1983, only 5 out of 19 state governments paid their full 10 percent grant to the local authorities. Furthermore, 14 of 19 state governments deducted substantial proportions of the federal government grants due to local authorities and unilaterally diverted them to state services. This is particularly significant because local governments raise less than 20 percent of their revenue from local taxes and charges and must depend heavily on state and federal governments. The local authorities have little autonomy, and, in the final analysis, they can do little that is not in line with the wishes of the state governments. Thus, Nigeria is a case where the state governments wield unusual power, and attempts to implement a significant fiscal role for local government have failed.

Bangladesh: Strong Decentralization in a Unitary State[6]

Bangladesh is an interesting case because it is a unitary central government with a highly developed system of local government. There is a long history of local government on the Indian subcontinent, which dates back to before the turn of the century under British rule. Bangladesh has carried on the tradition of local government, making various refinements in the direction of decentralization over the years. Although recent research has indicated that rural local governments do not have a sufficient degree of fiscal autonomy to discharge all of their potential responsibilities properly, Bangladesh has a degree of local participation in decision-making that is enjoyed by few developing countries with unitary governments.

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[6] The information on Bangladesh comes from Schroeder and Maniruzzman (1984).

There are four types of local government in Bangladesh. The zilla parishad is geographically identical to the district, which is the key administrative division of the central government. The upazila parishad corresponds to the thana, which is a subdivision of the central government district. These two types of local government have strong links to the central government and its ministries. Central government officials are dominant members of the zilla parishad councils, although there are plans to introduce a greater degree of elected representation. The upazila parishad council has more direct local representation, although it has no employees of its own and relies on central government staff to carry out the council's functions.

Union parishads are the third type of local government in Bangladesh. These local authorities cover rural subdivisions of the upazila parishads. These are politically autonomous from the central government in the sense that nearly all of the members of their councils are directly elected in the local jurisdiction. This is also largely true of the paurashavas, which are the fourth type of local authority. These are the form of local government in the urban areas of Bangladesh.

The zilla, upazila, and union parishads are somewhat integrated local governments, which are responsible for a hierarchy of services in the rural areas. Although there are many possible responsibilities for the zilla parishads, their prime responsibility in practice is for public works, particularly roads for the district area. They also have local responsibility for a national works programme, and make some expenditures on education, agriculture, public health, and social welfare and culture. The levels of local government below the zilla parishad, despite a more democratic political organization, do not have the financial resources to play a major role in service provision. The upazila parishads cover smaller areas within the zilla parishads and help with many of the zilla parishad responsibilities in their jurisdictions. Union parishads are supposed to be assigned responsibility for 40 different functions. Due to serious financial constraints, however, they often do little more than settle local disputes, try to document local agricultural and irrigation needs, and provide some road maintenance services.

Zilla parishads get most of their revenue from taxes, particularly a tax on immovable property. They also get some earned income from enterprises, and they depend on the central government for about 35 percent of their revenue. Upazila parishads get their revenue from markets, fishponds, and local businesses. They also get fees for various licenses, but are overwhelmingly dependent on central government grants. Union parishads get their income from taxes on property in urban centers and various types of small fees. The also get around 40 percent of their revenue from central government grants.

The paurashavas in the urban areas are completely independent of the zilla-upazila-union parashad system of local government in the rural areas. They are responsible for a wide range of traditional urban services, including health, sanitation and sewerage, conservancy, markets and slaughterhouses, education, etc. The two main sources of revenue are the urban property tax and the octroi, which is essentially a tax on goods brought into the municipality. These two taxes accounted for about 65 percent of paurashava income in 1981, with most of the rest coming from miscellaneous taxes, tolls, and service fees. The paurashavas are fairly independent financially, with only about 10 percent of total income coming from the central government in 1981.

Thus, Bangladesh has a substantial and largely independent system of self-government in its urban areas. The local government system in the rural areas is less independent, particularly financially. Even with central government grants, the rural local governments cannot adequately provide the services for which they are responsible. There is, however, a degree of representation and participation in local government which is fairly rare in the developing countries with unitary central governments. Despite a lack of financial resources for local authorities, the local government system in Bangladesh might serve as a model for other developing countries, although it might need to be simplified for many other places.

The Sudan: Strong Central Control in a Multitiered Unitary State[7]

The development of modern Sudan in the colonial and post-independence eras has seen the rise and fall of a variety of local government systems. As the largest country in Africa in terms of area, the difficult issue of decentralized administration has long been a major problem for government. The situation has been complicated by the division of the country into an Islamic north and a southern area dominated by Christians and followers of traditional African religions. The country was able to remain united under colonial rule, but the power struggle between the north and the south has caused turmoil since independence and is the cause of the current Sudanese People's Liberation Army (SPLA) civil war against the Islamic government. This case is interesting because it clearly points to the problems that can evolve when a colonial power imposes a system of unitary government over a geographic area that has no basis for unity.

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[7] The information for the Sudan comes from: Presidency of the Republic of the Sudan (1980); Norris (1983); Nooi (1987); and, Marouf (1987). The author also interviewed Fouad Eid Ali, Undersecretary, and Mohamed Ahmed Osman Marouf, Director of Training, Ministry of Local Government, Khartoum. The interviews were conducted in July 1987 at the International Union of Local Authorities (IULA) Conference on Local Government in Africa held in Mombasa, Kenya, in July, 1987.

Local government reform became important in the early 1970s. During the course of that decade, the number of local authorities increased from 86 to 5,600. The powers of central government ministries in the provinces were curtailed and the Ministry of Local Government dissolved. Control of the local authorities was handed over to the provincial commissioners. Unfortunately, most of the provincial commissioners kept the power at their level and did not extend decentralization to the lower tiers.

Attempts at reform again occurred in 1980 and 1981 with the passage of the Regional Government Act and the Local Government Act. The provinces became regions under the leadership of governors, who are regional ministers of the central government, and regional governments became known as people's regional councils. Regional government was given the power to license elected local government councils, which were corporate bodies with independent budgets and autonomous powers. A Ministry of Local Government was re-established to support the new decentralization initiatives.

After the uprising of April, 1985, the people's regional councils and local government councils were dissolved. They were replaced by appointed regional and local administrative committees, which are supposed to perform the same duties and functions as the regional and local governments they replaced. The central government is currently studying the issue of what to do about local government in the future.

Decentralized levels of government are responsible for a wide variety of services in the Sudan. Regional governments have primary responsibility for health and secondary education, while local governments provide water, sanitation, works, primary education, and other basic services. Local governments do have the power to collect certain fees and taxes, the most important of which are the immovable property and personal property taxes, but the revenue is considered to be the property of the central government. Local governments are highly dependent on the central government--80 percent of their income comes from central government grants. Local governments are not allowed to borrow from any source.

Despite a number of attempts to decentralize, Sudan remains a country with a highly centralized public sector. Little remains of the decentralization efforts except the shell of decentralized institutions. Before central government administrative committees took over the responsibilities of regional and local governments, there was a fair degree of local autonomy and participation through the election of semi-independent councils, but there was also a high degree of financial dependence on the central government. During the current civil war, there has been a clear reversion towards centralization.

Papua New Guinea: Extreme Fiscal Dependence of Strong Local Governments in a Unitary State[8]

Papua New Guinea was highly centralized and had a very weak system of local government until the late 1970s. In 1977, the central government replaced the district administration system with a provincial system, which formed the basis for local government. The provinces were to be run by powerful elected provincial assemblies and executive councils. Provincial governments were given full legislative and managerial responsibilities for a wide range of local functions, including public works, hospitals, and education. In addition, they were assigned some responsibility for joint central-local functions, and they were given access to a number of local taxes, the major one being the sales tax. The central government also provides substantial transfers, including: a significant administrative functions grant; 1.25 percent of the value of export goods produced in the provinces; and, all revenues from license fees and royalties collected by the central government in the province.

The 19 provincial governments in Papua New Guinea are overwhelmingly dependent on the central government for their income. In 1978, provincial own-source revenues accounted for an average of only 6 percent of total provincial revenue.

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[8] The information on Papua New Guinea comes from: Conyers and Westcott (1979) Cochrane (1983); and, Rondinelli (1983).

By 1981, the situation had improved very slightly: 8.5 percent of provincial revenues were generated by provincial taxes. During the 1978-81 period, unconditional grants from the central government to the provincial councils increased by 65 percent, while other types of central government transfers to the provinces increased by 45 percent. In general, central government transfers to provincial governments account for 20 to 25 percent of total central government expenditures in a given year.

Thus, Papua New Guinea has a highly developed system of provincial self-government with a significant degree of autonomy. Fiscally, however, the provincial councils are dependent on the central government for the vast majority of their income. Some analysts might be highly critical of this arrangement, but it is possible to argue that the system works very well and is appropriate for a small country, such as Papua New Guinea.

Zimbabwe: Developing Decentralized Government in a Unitary State[9]

Zimbabwe is a new country which is still in the process

[9] The information on Zimbabwe came from a presentation at the International Union of Local Authorities Conference on Local Government in Africa held in Mombasa, Kenya in July, 1987. The presentation was given by B. Mtandwa, Mayor of Kwekwe and Deputy President of the Urban Councils Association of Zimbabwe. Interviews were also conducted with the speaker and several other members of the Zimbabwe delegation, including J.S. Moyo, Ministry of Local Government, Harare.

of developing its system of government. The former white minority-ruled Rhodesia has only been known as Zimbabwe since 1980. The former government of Ian Smith had retained the colonial system of local government. Under this system, there were 242 African councils. The armed struggle, which eventually led to the rise of a black majority government under Robert Mugabe, basically destroyed the African council system, which the Africans considered to be a puppet extension of the racist regime.

Since that time, the government of Zimbabwe has been trying to implement a relatively strong and autonomous system of local government. There are currently 126 local authorities in Zimbabwe of three different types: urban councils, district councils, and rural councils. These do not overlap jurisdictionally and are all empowered to provide the same types of services.

There is a good degree of participation in local government in Zimbabwe. For every 500 people there is a village development committee. Ten of these committees form a ward within the local authority in which they are situated, and each ward is supposed to elect a councillor to the local council.

Local authorities in Zimbabwe are responsible for a wide variety of public services. These include: fire, police, ambulance services, planning, health inspection, roads, health, education, social welfare, water, sewerage, waste management, and refuse collection. Of course, not all of these services are provided by all local authorities, but most of these services are provided in the urban councils.

The local authorities in Zimbabwe have access to a wide variety of revenue sources, including property rents and rates, vehicle and shop licenses, housing rents, service charges, education fees, and health fees (for those who earn more than a certain income). Local authorities may also earn income from various public enterprises, including liquor trading, ranching, crop farming, and the building of factory and commercial shells for investors. Councils are free to seek loans from both the central government and on the open market.

There is some degree of financial and functional independence among Zimbabwean local authorities, particularly in the urban areas. District councils rely on the central government for about 50 percent of their revenue, while rural councils get 30 to 40 percent of their income from central government grants. Urban councils are much more self-sufficient, relying on the central government for only 5 to 20 percent of their revenue. The Ministry of Local Government and Urban and Regional Development has regulatory power over the local authorities, but many of its policies are designed to increase the capacity and self-sufficiency of local governments.

Thus, Zimbabwe is a case of a new system which is trying from the beginning to carve out a substantial fiscal role for local government. The local authorities in this country are empowered with significant service provision responsibilities and a variety of revenue sources, and they seem to be developing with remarkable speed.

Botswana: Reducing Local Government Fiscal Autonomy in a Unitary State[10]

Unlike Zimbabwe and other developing countries that are trying to strengthen local government, Botswana seems to be moving in the opposite direction. Botswana, in contrast to most former British colonies, never had a modern western system of local government imposed on it during the colonial years. It was not until independence was attained in 1966 that a system of local government was instituted. A council was set up in each district, the decentralized administrative division of the central government. Several town councils were also established in urban areas.

Local authorities in Botswana are technically responsible for a wide variety of public services, including primary education, basic health services and facilities, rural road maintenance, and village water supplies. They also have access to a variety of local taxes, the most

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[10] The information on Botswana came from Reilly (1983) and Wallis (1987). Interviews were also conducted of local government officials from Botswana attending the International Union of Local Authorities (IULA) Conference on Local Government in Africa held in Mombasa, Kenya in July, 1987.

productive of which is the property tax. The central government has a system of deficit grants to local authorities that automatically make up any revenue shortfall in local authority budgets.

The system of participation through local government in Botswana is often considered to be one of the best in Africa. However, the degree of fiscal autonomy is relatively small and seems to be in the process of being cut back further by the central government. The local authorities are under strict control by the Ministry of Local Government and Lands, which must approve most local authority revenue-raising and spending activities. As of 1988, the central government is taking over all local authority taxes. Thus, local authorities in Botswana will be entirely dependent on central government for their income.

Despite being considered a model for political decentralization in Africa, Botswana is one of the few developing countries that seems to be explicitly and openly undermining the fiscal powers of local authorities at a time when many developing countries are at least talking about decentralization.

Peru: Extreme Centralization in a Unitary State[11]

The public sector in Peru is among the more highly centralized of the world's developing countries, with the

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[11] The information for Peru comes from Greytak (1982).

central government collecting most of the public sector revenues and also doing most of the spending. In 1979, central government expenditures accounted for over 96 percent of total public sector spending.

Most public services in Peru are planned and provided by ministries and public enterprises under the central government. This is true for water, sewerage and sanitation, roads, public health, electricity, and other major services, both in the rural and urban areas. Although local authorities share some of these responsibilities in name, in practice they have neither the resources nor the staff to have a significant independent impact on service provision.

Peru is divided into three levels of local government. The country is divided into 24 departments, which are, in turn, subdivided into 113 provinces. The provinces are further subdivided into 930 districts. The provinces and districts are most important in terms of service provision. All types of local government in Peru are primarily rural in nature, although they do provide services in the urban areas. Capital cities in the provinces, for example, fall under the jurisdiction of the provincial local government.

Peruvian local governments, in fact, have clear legal authority to provide services and raise revenue. In addition to having a role to play in the provision of the services named above, local authorities are allowed to raise revenue from user charges, the sale of goods and services, and various taxes, the most important of which is the tax on immovable property.

At one time, the local governments in Peru played a more important role than they do today. During the 1970s, the growth of the local government sector lagged behind the overall growth of the public sector, leading to a decline in the overall importance of local government. In 1979, local government accounted for only 3.7 percent of total government expenditure and was responsible for substantially less than one percent of total capital spending by the government and public enterprises. In the same year, the largest single source of local government revenue was transfers from the central government. These accounted for 34 percent of total local government income.

Thus, Peru is a country in which the local government plays a relatively minor fiscal role in the public sector system. It is particularly noteworthy for its lack of independent local authorities in its urban areas. The small role of decentralized government in Peru is not unusual in developing countries, particularly among those in Africa and parts of Asia. It is, however, one of the most highly centralized states in Latin America. Efforts are underway to attempt to increase autonomy at the local level in Peru, but it is not clear how successful they will be.

Summary of Cases

The cases discussed in this chapter are presented in summary form in Table 2.3. This information clearly demonstrates the diversity of local government systems in developing countries along several important dimensions. The countries range from Brazil, a federal system whose state and local governments have moderate to high revenue self-sufficiency and decision-making autonomy, to Sudan, a unitary system whose regional and local governments have little revenue self-sufficiency and decision-making autonomy.

Between these two extremes, there are a variety of different cases that highlight particular aspects of local government systems in developing countries: Nigeria, with strong state, but weak local, government; Papua New Guinea, with regional governments that are highly dependent on the central government for revenue, but largely independent in making expenditure decisions; Peru, where local governments have moderate revenue self-sufficiency but little decision-making autonomy; Bangladesh, with strong urban but weaker rural local governments; Zimbabwe, where a new system of local government with an increasing degree of fiscal and political autonomy is being instituted; and, Botswana, where decision-making autonomy is high but revenue self-sufficiency is declining.

TABLE 2.3

DIVERSITY OF LOCAL GOVERNMENT SYSTEMS:
SUMMARY INFORMATION FOR EIGHT DEVELOPING COUNTRIES

Country Name	Type of System	Decentralized Government Types[1]	Revenue Self-Sufficiency[2]	Decision Making Autonomy[3]
BRAZIL	Federal	State Local	High Moderate	Moderate Moderate
NIGERIA	Federal	State Local	Moderate Low	High Low
BANGLADESH	Unitary	Rural Urban	Moderate High	Low Moderate
SUDAN	Unitary	Regional Local	Low Low	Low Low
PAPUA NEW GUINEA	Unitary	Regional	Low	High
ZIMBABWE	Unitary	Rural Urban	Moderate High	Moderate Moderate
BOTSWANA	Unitary	Local	Low	High
PERU	Unitary	Local	Moderate	Low

[1] Some countries have more types of local governments than those indicated, but detailed information was not available about the different types.

[2] The rating of some countries on revenue self-sufficiency is sometimes based on general impressions rather than data. These ratings are for rough comparative purposes only.

[3] The rating of local authorities on decision-making autonomy is based on impressionistic and incomplete information. These ratings are intended for rough comparative purposes only.

Summary of Issues Regarding Local Government Diversity

In contrast to the situation 10 years ago, there does seem to be a trend in many developing countries towards strengthening local authorities, even in some areas where centralization has long been the rule. As one observer of the situation put it: "In practice this means local governments are being given a larger share of total public income; central controls over local governments are being eased; representative local governments are being re-established; municipal credit and technical assistance programmes and local government associations are being created; and popular participation in planning is emerging."[12]

Although this may be true in many countries, it is clear that policies for strengthening local authorities are taking very different forms in different developing countries. This is true not only because government systems differ widely, but also because the cultural and political climates are so diverse. Even countries with similar political systems have very different ways of organizing and operating their local governments. It is also clear from the cases discussed above that not all countries are likely to strengthen local authorities in a meaningful way, and a few are actually moving in the direction of greater centralization despite the

[12] This quote is taken from an editorial in Planning and Administration, Vol. 12, No. 2 (Autumn 1985).

rhetoric of reform.

It is very difficult to summarize the different ways in which local government is organized in developing countries because of the great variety of roles that local authorities are called on to play. It is reasonable to say, however, that there are a set of basic dimensions along which local authorities differ. First, government systems differ in the number of decentralized levels of government that exist and the constitutionally and legislatively mandated administrative relationships they have among each other. Second, local authorities differ in their degree of political decentralization and grassroots legitimacy. Some local authorities have significant political power and are popularly elected, while others are appointed councils that follow the directives of a more centralized level of government. Third, local authorities differ in the degree to which they have autonomy in revenue-raising and expenditure decision-making. Some have significant autonomy in both, others in one area, and still others have little autonomy of any sort. Fourth, local authority systems differ in the average degree of fiscal capacity relative to service responsibilities. Local authorities in some developing countries can more or less finance their designated services, while others do not have the ability to raise sufficient revenue to do so. In some cases, the central government steps in with financial assistance, while in others the revenue shortfalls remain. Finally, governments in developing countries vary in their attitudes about centralization. Many local government systems are being strengthened, but in some developing countries the degree of centralization is actually increasing, sometimes in violation of how the constitution and relevant legislation say the decentralized government sector is supposed to be organized.

This chapter has documented the diversity of local government systems and fiscal roles in developing countries. This establishes a broad context for defining a framework to analyze the fiscal role of local government in developing countries, which is the central focus of the next chapter.

CHAPTER 3

FISCAL ROLE OF LOCAL GOVERNMENT IN DEVELOPING COUNTRIES: A FRAMEWORK FOR ANALYSIS AND EVALUATION

The diversity of local government systems and operations in the developing world is tremendous, as was discussed and documented in Chapter 2. This extreme diversity introduces serious complications into an analysis of the fiscal role of local government in these areas. In spite of these complications, however, the public finance literature has certain insights to offer on the fiscal role of local government in developing countries. In this chapter, this literature will be briefly reviewed and its relevance for developing countries evaluated as a prelude to outlining a basic framework for analyzing and evaluating the fiscal role of local government in the developing world.

Public Finance Background

Before the issue of defining a fiscal role for local government can be analyzed, it is first necessary to identify the economic role that government as a whole has to play. The early welfare economists demonstrated that, under the usual assumptions of perfect competition, a market economy generates a Pareto-efficient allocation of resources without any government intervention. The private-goods welfare economics model was extended to the case in which there is market failure and public goods are provided by the government. In two classic articles, Samuelson (1954 and 1955) showed that, under certain strict assumptions, a properly functioning market economy will generate a Pareto-optimal allocation of resources between public and private goods.[1] He also demonstrated, however, that there was a frontier of Pareto-optimal solutions, and that it was necessary to define a welfare function that embodies societal preferences in order to select the Pareto-optimal mix of private and public goods that maximizes social welfare. This suggested the need for a political decision-making process capable of defining a distribution of resources deemed "fair" or "desirable" by society, even in a case where the strict assumptions of the model hold.

The variety of market imperfections or failures that exist in any modern economy justify some economic role for government on allocation grounds. Public interference in the economy in order to allocate resources more efficiently is

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[1] Samuelson was building on earlier writings in welfare economics that defined the efficiency conditions for pareto-optimality in a world with only private goods. He demonstrated that the efficiency conditions for the public and private goods case differ from those in the private goods only case. The efficient solution for private goods exists when the marginal rates of substitution in consumption are equal for all consumers and equal to the marginal rate of transformation in production. Where public and private goods are involved, the fact that public goods are non-rival in consumption must be taken into account. All consumers are provided with an equal amount of the public good, so that the marginal rates of substitution of public for private goods may differ. Because consumers share in the consumption of the public good, the marginal rate of transformation in production must equal the sum of the marginal rates of substitution in consumption for all consumers.

sanctioned by economists for three principal reasons. First, in cases where there are natural monopolies (or oligopolies), resources may be more efficiently allocated if the government regulates or operates these enterprises. Second, when production or consumption of a good or service generates external costs or benefits that accrue to other producers or consumers, the market-pricing mechanism fails, and resources will be over- or under-allocated in these markets. In such cases, the government can regulate or provide incentives for the private sector to internalize costs and benefits. Finally, there is the case of public goods, which the private market fails to provide or provides suboptimally because of their nonrival and non-excludable nature. Pure public goods are extremely rare--most goods provided by governments are impure, i.e., are to some extent rival and excludable. There are also cases of merit goods, which generate such important external benefits that the government decides to provide them because they would otherwise be provided at suboptimal levels by the market.[2]

Providing optimal levels of public goods is complicated by the "free rider" problem: people have no incentive to reveal their true preferences for public goods because they will still enjoy them if other people are willing to pay.

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[2] The market may also fail when information is expensive and/or imperfect. When individuals do not have the information required to make well-informed decisions in the marketplace, inefficient patterns of resource allocation are likely to emerge.

This results in the need for use of governmental powers of coercion to extract taxes to finance public goods. The selection of an optimal combination of public goods and taxes, like the identification of an optimal distribution of income, is basically left to the political process.[3] Public choice theory has demonstrated that, under special conditions, the outcome of a majority voting process reflects the preferences of the median voter and results in a stable solution to the problem of making collective decisions. A number of theorists have attempted to deal with other aspects of the complicated problem of public choice, including intensity of preferences, logrolling, representative democracy, and bureaucratic decision-making.

The final justification for government interference in the economy is that market-economies are not inherently self-regulating and require government intervention for <u>stabilization</u> purposes.[4] After the stock market crash of 1929 and the Great Depression which followed it, a stabilization role for government was somewhat reluctantly acknowledged by mainstream economists. Roosevelt's New Deal programs ushered in a new era of government intervention in the economy. "Keynesian Economics," however, was not fully

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[3] An excellent review of public choice theory is found in Mueller (1976).

[4] The allocation, distribution and stabilization roles for the public sector were first elaborated as a group of functions by Musgrave (1959) in his seminal public finance text.

and explicitly incorporated into mainstream economics until the Kennedy years, when discretionary fiscal policy formally emerged as official government policy.[5] The Keynesians justified the need for the government to use monetary, tax, and spending policy to help moderate the effects of regular cyclical upturns and downturns in a market economy. Government may use these policy instruments to move against the direction of the cycle by injecting purchasing power into the economy during recessionary downturns and withdrawing purchasing power from the economy during inflationary upswings. As the international economy became more interrelated, stabilization needs also dictated a more active government role in the management of exchange rates and the international balance-of-payments. During the past decade there have been popularized critics of Keynesian economics and a great deal of anti-Keynesian rhetoric by conservative politicians. Nevertheless, few modern macroeconomists would deny that the public sector must serve as an agent of macroeconomic stabilization.

In summary, mainstream economics assigns three major functions to the public sector. Government intervention is justified to provide a more efficient allocation of resources

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[5] Not all followers of Keynes would accept as adequate the stabilization role for government defined by the mainstream macroeconomists. The post-Keynesians would argue that mainstream economists have not fully acknowledged the instability, that, according to Keynes, is inherent in a capitalist economy, nor the political economy basis for this instability.

when there are market failures. It is also acceptable for government to implement policies to affect the distribution of income, according to some politically defined notion of what constitutes a fair income distribution. Finally, government is expected to pursue various types of countercyclical policies in order to stabilize macroeconomic fluctuations.

Theories of the Fiscal Role of Local Government

The theories briefly outlined above were applied by public finance economists to the issue of decentralized government. An appropriate role for local government in developed countries has traditionally been defined by economists using a basic theory of fiscal decentralization known as fiscal federalism.[6] Drawing on the standard model of public sector responsibility for stabilization, distribution, and allocation, the decentralization model provides economic guidelines for dividing these functions among different levels of government. In addition, the model presents guidelines for designing an optimal local revenue system.

Stabilization

Primary responsibility for stabilization is generally

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[6] The theory of fiscal federalism is set forth in detail in Oates (1972).

assigned to the central government because stabilization activities are considered to be essentially macroeconomic. Monetary policy must be managed at the national level because of the problems that would result if subnational jurisdictions had their own money supply and/or control over monetary policy. In addition, local economies are likely to be highly open, suggesting that leakages from a marginal dollar of private spending are likely to be substantial. Thus, the expenditure multiplier (the reciprocal of the sum of the marginal propensity to save and the marginal propensity to import out of income) would be small, and the expansionary effects of local fiscal policy, such as a local tax cut, would be dissipated into other areas. Finally, the use of Keynesian deficit finance policies would not be desirable at the local level. Such debt is often held by individuals external to the local jurisdiction, and the repayment of such debt will involve the transfer of real income to individuals outside the local area.[7]

The standard arguments for assigning the stabilization function to the central government have recently been challenged. Gramlich (1987) has argued that, at least in the case of the United States, new macroeconomic developments and large federal deficits in recent years have greatly

[7] Of course, it must be acknowledged that central government debt can also be held externally to a significant extent. In the case of some developing and developed countries, the problems that this can generate have been fairly evident in recent years.

constrained the ability of the federal government to pursue countercyclical policy. He also demonstrates that state governments have successfully played a greater role in pursuing countercyclical policies than they did in the past. Although some of these findings, particularly those relating to changes in macroeconomic conditions, may be generalizable to other countries, the ability of decentralized government stabilization policy to have the desired effects will depend on a variety of factors in any given country, including the importance of decentralized governments in the national economy.

Distribution

The fiscal federalism model places responsibility for distribution in large part with the central government primarily because of the problems that would be expected to result from factor mobility if local redistribution programs were undertaken. Local redistribution programs could induce wealthy residents and businesses to move out of a jurisdiction practicing redistribution, while poor individuals eligible for benefits would move in, thereby undermining the redistributive base. This would particularly be a problem for small jurisdictions and especially where local redistribution programs were not widespread and fairly similar across jurisdictions.

Other analysts, such as Pauly (1973) and Tresch (1981), have suggested that income redistribution may raise the utility of higher income people and that taxpayers should and will try to raise the incomes of the poor primarily in their own area. Gramlich (1987) has argued that in recent years, state governments in the United States have been playing a greater and successful role in implementing redistribution policies. The question of central versus local primacy in redistribution policies is difficult to resolve empirically, but the mobility issue continues to be an important concern, as does the existence of interjurisdictional income disparities in a given country. These disparities suggest that, if redistribution responsibility is decentralized, some wealthier areas will be better able to effect meaningful income redistribution than their poorer counterparts. Some decentralized redistribution probably occurs in many countries because local governments may provide services that benefit the poor, who may pay few or no taxes.

Allocation

The role of decentralized levels of government in the allocation function is very substantial. The basic idea behind this assertion is that there is not likely to be uniform demand for many public goods and services across large geographic areas. If this is the case, there would be a misallocation of resources if uniform levels of services were to be provided across large jurisdictions. Welfare gains could be enhanced through decentralization because residents in the decentralized jurisdictions could choose the mix of public goods and taxes that best conforms with their preferences. In the absence of a market and competitive pricing, community-wide demand would obviously be made through the collective decision-making process, i.e., voting. In this framework, a fragmented pattern of jurisdictions is preferable to a system of large, all-purpose authorities. This is true not only because of the preference differentiation issue, but also because in smaller jurisdictions, expenditure decisions are tied more closely to real resource costs. In addition, when there are a large number of decentralized governments providing services, there is likely to be greater experimentation and innovation in the provision of local public goods, potentially leading to improvements in overall resource productivity.

Extensions of the logic of preference variations suggest that in a system where there are opportunities for mobility, people will move to an area where a local government provides their preferred mix of public services. This produces a market-like solution to the local service provision problem. An equilibrium occurs when people distribute themselves across differing communities in such a way that there is no incentive for anyone to move, i.e., everyone is satisfied with the services being provided in the jurisdiction in which they reside.[8] This "voting-with-the-feet" theory is based on a variety of strict and unrealistic assumptions, e.g., no externalities, perfect mobility, perfect information about public goods and services in a very large number of heterogeneous communities, zero government fixed costs, and constant costs of production. Nevertheless, it is useful conceptually, and the results of the relaxing the strict assumptions can be analyzed.[9]

There are important exceptions to the general rule of decentralizing to maximize efficiency in service provision. Some services, such as utilities and transportation systems, exhibit economies of scale, and, in such cases, it is more efficient to provide these services at a more centralized level or through a cooperative agreement of local authorities.[10] In addition, there are cases, such as water supply, in which the provision of particular services generates interjurisdictional externalities. In such cases,

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[8] This theory was set forth by Tiebout (1956) during the early development of public finance theory and prior to the articulation of the fiscal federalism theory. However, it actually fits in well under the discussion of efficiency in the allocation of resources and so is placed under the umbrella of fiscal federalism.

[9] There has been a variety of theoretical writing and empirical research on the fiscal federalism and Tiebout local government theories. Much of this work is summarized, discussed, critiqued, and analyzed in King (1984).

[10] It is technically efficient to assign service provision to a larger jurisdiction only if the cost savings from joint consumption outweigh the potential welfare loss involved in providing the good or service over a wider jurisdiction where preferences may be less homogeneous.

resource allocation is more efficient when the service is provided more centrally, cooperatively, or with central coordination. The ideal service provision area is one that just leads to an internalization of externalities.

Optimal service provision area is a very complicated issue, because it may vary greatly for different public goods and may in few or no cases correspond exactly to the boundaries of existing political jurisdictions. The welfare gains from establishing levels of government or independent authorities with efficient boundaries for providing a particular public good or goods must be weighed against the costs involved in having a larger number of jurisdictions. It may often be more practical and efficient to use intergovernmental grants to subsidize goods that exhibit positive externalities or to establish cooperative arrangements among existing government units in order to internalize externalities and/or capture economies of scale.

Oates (1972, p. 19) defines the central theoretical problem of fiscal federalism as: "the determination of the optimal structure of the public sector in terms of the assignment of decision-making responsibility for specific functions to the proper geographic subsets of society." This clearly implies that economic or fiscal federalism is different from political federalism, and that it may necessitate cooperative agreements among decentralized political jurisdictions, creation by the central government of regional or special authorities for provision of specific services, or provision, subsidy, or regulation of a particular service by a more centralized level of government. Because the efficient service area may not correspond to existing political jurisdictions and is theoretically independent of political considerations, the assignment of responsibility guidelines based on the theory of fiscal federalism can be applied even in countries where a federal political system does not exist.

Revenue-Raising System

Drawing on mainstream public finance theory, the fiscal federalism model sets forth guidelines for designing an optimal tax system to finance decentralized government functions. The guidelines explicitly incorporate spatial dimensions of a local tax system into the analysis. According to Oates (1972), there are four basic guidelines to be followed:

1. Local government taxes should be neutral, i.e., avoid excess burden. Local governments should select a set of taxes that extract the resources required to met their responsibilities but which have as few undesirable side effects on the operation of the economic system as possible. A tax is neutral when it does not alter the terms on which consumers or producers choose among alternative economic activities and possible locations for them. Such a tax

reduces private disposable income and leads to an alteration in expenditure patterns, requiring an adjustment in equilibrium prices and quantities in the system. It does not, however, alter relative prices and affect the basis on which economic decisions are made.

2) <u>The benefits and costs of local taxes should be clear to each individual in the local authority jurisdiction</u>. To the extent that local people understand how the tax revenue they pay is going to be used, they can make informed decisions, thereby increasing efficiency. This suggests the desirability of adherence to the benefit principle, which states that an individual should bear the costs of the benefits enjoyed from a particular good or service.

3) <u>The pattern of incidence of local taxes should be as equitable as possible</u>.[11] There are two basic types of equity, horizontal and vertical. Horizontal equity requires that people in similar circumstances be treated similarly by a particular tax. Vertical equity requires that people in different circumstances be treated differently. The latter is the basis for ability-to-pay taxation, whereby redistribution is effected because people of higher income or wealth pay proportionally more than people in less fortunate

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[11] The overall incidence of the tax and expenditure system is a better measure of equity than the incidence of the tax system alone. If, for example, a tax system is proportional, but expenditures highly favor lower income earners, the overall incidence of the system may be desirable even in the absence of a progressive tax system.

circumstances. The mobility problems that ability-to-pay taxes can cause across local jurisdictions have already been discussed.

It is important to note that a tradeoff exists between adherence to the benefit principle and the use of ability-to-pay taxation. The redistribution inherent in the latter violates the former, but this is often considered desirable in cases where a more equal distribution of income and basic public services is a national goal.

4) <u>Administration and compliance costs should be minimized</u>. Some taxes, such as a complex progressive income tax, are difficult and relatively expensive for government to administer and constituents to comply with. Taxes of this nature should be avoided by local government where possible because of limited local resources and administrative capacity and to minimize perverse incentives for those who pay taxes. Alternatively, local authorities can take advantage of the economies of scale in established central or regional government collection mechanisms to collect certain local taxes for which there are particularly significant economies of scale in collection.

In addition to these basic guidelines, several other factors and issues should be taken into consideration:

1) <u>The spatial dimension of decentralized public functions requires that issues related to local government competition and interdependence be explicitly taken into</u>

consideration. One of these issues, mobility, has already been touched upon in connection with ability-to-pay taxes and redistribution. The problem of mobility, however, is much broader. If particular taxes in one jurisdiction are higher than similar taxes in neighboring jurisdictions, affected taxpayers would be rational to move to the lower tax jurisdiction, all other things being equal. This results in a violation of the principle of neutrality and a loss in efficiency, because local taxes are affecting the basis on which individuals and firms make decisions about where to locate their economic activities.

Another spatial issue related to taxation is the degree to which a local government can export its taxes to residents of other jurisdictions. If, for example, nonresidents buy goods subject to a production or sales tax in a particular local authority, part of the burden of local taxes is shifted to other jurisdictions. Tax exporting is desirable from the point of view of the taxing jurisdiction, although it may create an incentive for some jurisdictions to push their output of public goods beyond the optimal level.

2) National goals regarding public service provision and equity may require central government intervention. To the extent that there are fiscal disparities across local governments in a particular country, there will be differences in the ability of some jurisdictions to provide public services. The national political process may decide

that local authorities should have more equal financial capacities than they do and/or that particular local services should be provided at a minimum level across all local authorities. In order to attain these goals, the central government can use block grants, which are unrestricted lump-sums, or categorical grants, which are restricted for particular priority uses. Intergovernmental grants can also be used to subsidize the provision of goods that involve positive externalities.

3) <u>It is possible and may be desirable to separate responsibility for revenue-raising and expenditure functions between levels of government</u>. In cases where there are unacceptable fiscal disparities across local authorities and/or highly inadequate revenue collection mechanisms at the local level, the central government can take primary responsibility for raising particular types of revenue and transfering it to the local governments. This can be consistent with the fiscal federalism model's emphasis on decentralizing the allocation function if sufficient local government autonomy over expenditure decisions is maintained.

4) <u>The desired criteria to use for assigning revenue sources to local authorities will generally differ from the point of view of central and local governments</u> [Bahl and Linn (1983), p. 183]. From the central government point of view, the most important criteria are likely to be: (a) limit local competition for important national tax bases; (b) limit local

use of taxes whose burden is exportable to residents of other jurisdictions; (c) provide local authorities with sufficiently buoyant revenues in order to limit demands on central government resources; (d) avoid local reliance on regressive taxes as much as possible; (e) encourage the use of taxes that can be easily administered at the local level; and, (f) encourage the use of taxes that closely reflect the costs of infrastructure and congestion.

Local governments are likely to agree more or less with criteria (c) through (f), and will be particularly concerned with having taxes that are buoyant and easily administered. However, local authorities are likely to have exactly the opposite priorities from those reflected in criteria (a) and (b). They would almost certainly like to get a share of productive national tax bases, and it is in their interests, as noted earlier, to rely on taxes whose burden can be exported to other jurisdictions.

Relevance of the Fiscal Federalism Theory to Developing Countries

Although few developing countries are federal systems, the fiscal federalism model provides some useful insights into evaluating the role of local authorities in the developing world. Some of the basic assumptions of the model, however, do not always apply in underdeveloped countries, and the context in which the model must be applied may vary tremendously from the more-developed nations. The appropriateness of the model for application to developing countries, with an emphasis on allocation, is discussed in the following sections.

Stabilization

It is appropriate to assign to the central government responsibility for stabilization in developing countries for essentially the same reasons as in developed countries, but the case may be even stronger for the former. Macroeconomic fluctuations are often very severe in developing countries. Agricultural economies located in areas subject to severe and unpredictable variations in climate and which are heavily dependent on other countries for manufactured goods and credit are in a highly vulnerable position. Stabilization policies must be carefully planned and coordinated by well-trained and experienced people. In addition, local governments in developing countries often have only a very small role in the economy and the public sector, sometimes accounting for as little as a few percent of total government spending. The impact of their fiscal policies is therefore extremely limited. Finally, casual observation suggests that some types of local authorities in developing nations are highly sensitive to both cyclical and unpredictable economic fluctuations. They all but close down in some areas because of the extreme dependence of rural local authorities on taxes related to the level of economic activity (e.g., agricultural taxes, business license taxes, market fees) and their minor reliance on wealth-based taxes (land rates) and fee-for-service activities (water and sewerage charges).

Distribution

The distribution function is also best handled by the central government in developing countries, but not necessarily for the same reasons as in developed nations. Domestic mobility of the rich is likely to be less of an issue in developing countries. There are often only a few major cities that provide a reasonably high level of public services and wealth-responsive amenities for which scale factors are important. Thus, people do not have a great deal of choice about where to live if they wish to enjoy the standard of living of an urban center. It is true that there has been a dramatic growth of urban areas in some developing countries as poor rural peasants unable to make an acceptable living from rural subsistence agriculture flock to large urban settlements in search of employment. In some countries, however, tradition and cultural factors may be an important barrier to permanent relocation, a point that will be discussed more fully in the next section.

Despite the possibility of fewer problems with mobility in some less-developed countries, there is no case to be made for assigning substantial responsibility for distribution to local authorities. In many areas, the resources of local authorities are very limited and there are few possibilities for serious redistribution. The role of local authorities is also very limited in many developing countries, and they do not have the capacity to administer major redistributional programs. Finally, there are serious political constraints that may block attempts to redistribute wealth at a local level. In some places, prominent wealthy residents have a great deal of control over local authorities and would be unlikely to permit substantial and explicit local redistribution policies, although some local services may be redistributional in the sense that they benefit poorer residents.

Although a major redistributive role for local government is not likely, it is nonetheless possible in some developing countries for local authorities to be somewhat progressive in the way they finance local services. Taxes may be levied in such a way as to fall on those who have greater ability to pay them. In some countries, for example, most local taxes are raised from local businessmen in the form of land rates, trading license fees, and charges for water and sanitation services in urban centers. This revenue may be used to help provide basic services for the general population, including the urban poor and rural peasants, who may pay few or no taxes to the local authority. If such a system were the standard practice in local governments throughout the country, there would be little opportunity to avoid the taxes by moving to another location. Thus, some redistribution can take place at the local level without necessarily inducing undesirable efficiency effects.

Allocation

The issues surrounding assignment of responsibility for the allocation function in developing countries are extremely complex. The assumptions underlying the fiscal federalism theory may be violated by certain factors that are uniquely or particularly important in developing countries, and the interpretation of how the theory applies in particular cases may be greatly affected. A variety of factors--economic, environmental, cultural, and institutional--are often relevant. Although these considerations are highly interrelated and cannot always be classified neatly into such distinct classes, an examination of each category is useful to illustrate the major issues involved.

Economic Considerations

The general logic of the fiscal federalism decentralization model would suggest that there should be more local government if there is reason to believe that local preferences differ across space. A wide variety of tastes and preferences exist in wealthy industrialized nations, but there may be much less heterogeneity of preferences in the developing world because a majority of the population is very poor. This poverty cuts across urban and rural areas, occupations, tribes, and other dimensions that might be expected to influence preferences. The notion of willingness-to-pay may even be irrelevant for large segments of the population in developing countries. Many people in developing areas do not have the money to create effective demand for public services, and certain socioeconomic groups may not be subject to any significant taxation even if they benefit from public services. In many areas, the chief "preference" is likely to be for the provision of some minimum level of basic services. Particularly in very poor countries, this package of basic services may vary very little across local authorities except insofar as they differ along a few basic dimensions that affect the composition of the required service package, i.e., urban, rural agriculture-oriented, and rural livestock-oriented. The extent to which the level of services varies across local authorities with the same economic base may be largely a function of population or other size variables that affect demand. This greater homogeneity of preferences might suggest that there should be more central or regional government involvement over wider geographic areas. Although this is clearly true in some cases, it may be offset by other factors to be discussed later.

Bahl and Linn (1983) have argued that interjurisdictional externalities in metropolitan areas may be less important in developing countries than they are in the United States. This is true because those functions that tend to have the greatest spillover effects, such as education and health, tend to be the responsibility of the central government in developing countries. Even in cases where they are a local responsibility, the limited mobility of rural people in developing countries may result in less access to urban facilities for much of the population than is the case in developed countries. Finally, there is generally not as much jurisdictional fragmentation in the metropolitan areas of developing countries as there is in the developed ones, thus reducing the possibilities for problems with interjurisdictional externalities.

Environmental Considerations

Public services serve as inputs to the production process, and production needs may differ dramatically across local authorities due to a diversity of opportunities and constraints that result from natural and planned environmental factors. At the most aggregate level, preferences and needs differ markedly between rural and urban areas and between different types of rural areas in the typical developing country. Urban areas require traditional urban services such as roads, water, and sanitation. Rural areas primarily require services that support production and marketing of rural economic activities, which may be largely livestock-related in some areas and largely agriculture-related in others. Thus, differences in preferences and needs are strongly related to variations in the composition of economic activity that arise, to a great extent, from agro-ecological conditions.

Environmental factors may dominate the determination of the types of industry and other economic activities that operate in particular urban areas as well as the nature and level of public services required to support these activities. One urban area may engage in activities that require street lights, a high level of electricity, particular types of sanitation services, etc., while another may not. Similarly, environmental factors determine the types of crops and livestock that can be raised in a particular rural area and the nature, quality, and quantity of public services required to support these activities. To the extent that great differences in environmental factors have a major impact on the type and level of economic activities conducted in different local authorities, preferences for public services will vary across space and the case for local government is strengthened. Such differences may be very prominent in some developing countries because of extreme differences in agro-ecological conditions in tropical regions.

Another complicating factor in the analysis is the heterogeneity of the population within particular local authorities in some developing countries, which is due both to natural environmental factors and boundary decisions made by the central government.[12] Urban local authorities may have 100 percent of their population living in truly urbanized areas, or a significant portion may live in rural areas within the urban authorities' boundaries. In developing countries, towns sometimes serve mainly as trading centers, with few residents living in the town center. This can greatly affect the types of services required and the area over which they should be provided. Similarly, some rural local authorities may have most of their populations living in rural areas, while others may have significant concentrations of people in urban trading centers located within their jurisdictions. The type and extent of services required in local authorities may thus be extremely diverse, leading to heterogeneous preferences for public services <u>within</u> a particular local authority.

In many of the developing countries, particularly the larger and less-developed ones, settlements requiring local public services are located far apart and/or are connected by poor roads and inadequate transportation services. This

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[12] Natural environmental factors may be less important than boundary considerations, but there are clear cases where they will be important. In a rural local authority, for example, the existence of a good water supply at a particular site may lead to a concentration of population around this site and the development of an urban center with a need for urban services. In the absence of such a site, the population of a rural local authority may have to be more dispersed or nomadic in order to satisfy their water needs.

geographic inaccessibility makes regular central or regional government intervention and monitoring very difficult and expensive in remote regions even under the best of circumstances. Thus, in some countries, centralization or regionalization of service provision would not be very effective, even if preferences are relatively homogeneous. This strengthens the case for service provision by local authorities.

Cultural Considerations

The allocation aspect of the fiscal federalism model is based on the neoclassical notion of individual preferences. In many traditional societies in the third world, this is a culturally alien concept. Family and extended family obligations are often much more formal and demanding than those in the developed world. In addition, there are other important levels of social allegiance involving clan and tribal obligations; furthermore, there may be extreme restrictions imposed on individual choice because of caste, ethnic, or religious affiliations, and in some countries, gender is a major issue. All of these factors must be taken into consideration, and may be much more important than individual preferences in the decision-making process. If such social allegiances and restrictions predominate for most or all major cultural groups in a particular country, the individual preference basis of the fiscal federalism model is undermined and preferences may be more homogeneous over larger areas.

The traditional model of local government assumes a high degree of mobility in order that citizens can move to an area that provides their preferred mix of public goods and services. The mobility assumption is crucial to the model, whether individual or social group preferences are the basis for making decisions. In some developing countries, mobility may be greatly restricted among the majority of the population, primarily for cultural reasons.[13] Many indigenous people are unwilling to leave the area of their birth permanently. People who move do so largely in search of employment with little or no consideration given to taxes and public sector amenities, and many who move to urban areas maintain only temporary residence there. They leave their families in the home area and visit them as often as possible, fully intending to return to their homes to settle down after acquiring sufficient money. People may be more willing to move within the home area, but permanent relocation to other districts may be strongly resisted by people in some countries.[14] This factor, combined with the

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[13] Some of the rural-urban migration literature on developing countries hypothesizes that migration from rural to urban areas is a rural <u>household</u> decision to allocate <u>family</u> labor between the rural and urban economies. For example, see Huntington (1977).

[14] There is some evidence to indicate that migrants to urban areas in developing countries intend to return to their rural area of origin. Oucho (1986), for example, conducted a

basic needs versus varied preferences issue discussed earlier, suggest that "voting-with-the-feet" models are much less relevant in developing countries. In addition, to the extent that temporary migrants to urban areas remit much of their earnings to their home areas and live in very basic and/or temporary settlements, they may have only a minimal demand for urban public services in the places where they work.

Cultural factors may also sometimes complicate the issue of intra-jurisdictional diversity. Some major towns and trading centers in developing countries have grown up along tribal or ethnic territorial boundaries. Two different ethnic groups may coexist in the area around the trading center within the same political jurisdiction. Even though both groups may live on land with roughly the same potential, the two groups pursue very different livelihoods and live in different types of settlements largely because of tribal culture and tradition. For example, one group may be pastoralists who live semi-nomadically, while the other group may be farmers who live and work on fixed parcels of land. Thus, although the two groups live in the same agro-ecological zone and the same local authority, they have very

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study of rural-urban migration in Kisumu, Kenya. In interviewing migrants, he found that only 13.7 percent planned to stay in Kisumu permanently, while 15.8 percent expressed their intention to leave when they retired and another 50.2 percent planned to leave at some time in the future.

different public service needs because of their occupations and living arrangements.

Institutional, Legal, and Political Considerations

The allocation role of the public sector is often more extensive than it is in developed countries. Private sector institutions tend to be less self-sufficient and less organized in the developing world, and the government needs to undertake some essential functions in support of basic economic activities because other institutions do not provide them. There are often nationalized or parastatal industries and marketing institutions at the central government level, while some extended functions in less-developed countries are more local in nature. Some of these might include the provision of marketing facilities and support services, such as veterinary care and agricultural extension work. Thus, local government must often provide services that are not particularly "public" in nature.

The fiscal federalism theory stems from a sense of integrated local government in a developed government system. In some developing countries, local governments are token institutions. They exist outside of a central government administrative system that may have its own decentralized institutions. These often exist alongside of local authorities in the regions but may be much more powerful. The fiscal federalism model further assumes implicitly that local governments have sufficient constitutional and/or legal powers to enable them to discharge their appointed responsibilities, which may not be the case in some developing countries.

Local authorities in developing countries must operate under difficult conditions because of deficiencies in basic local institutions, which support the local revenue base and generate further development, and national institutions, which are poorly developed and may be overwhelmingly influenced by political considerations. In a developed country such as the United States, private property and homeownership are widespread, and some type of large-scale industry exists in much of the country, including what are considered "rural" areas. In developing countries, these factors, which are mainstays of the local revenue base in industrialized countries, may be much less important or inapplicable.

Although there are significant variations in levels of income and expenditure across local governments in the United States, it is fair to say that they provide a relatively standard set of services and have a relatively standard set of revenue sources available to them. This may not be true in a less-developed country; furthermore, the differences across local governments in the United States are largely self-assigned on the basis of local preferences or the result of some explainable factor, such as local wealth. In developing countries, these differences may be arbitrarily imposed on a local government by the central government bureaucracy, which may also impose a variety of other constraints and conditions on local authority operations. It is not unusual, for example, for there to be little correspondence between required services and permitted income sources, a situation that may lead to local authority financial crisis.

Limited resources are a significant intergovernmental constraint in less-developed countries. Even though sufficient resources to meet service obligations may not be available locally in all parts of developed countries, there are models that detail various methods of transferring income to the local governments, as well as revenue-sharing and other grant programmes that do so. In developing countries, redistributive intergovernmental grant programs may not exist because of limited central government resources or central government negligence towards local authorities. In cases where intergovernmental transfer programs do exist, they may be underfunded and the funds distributed according to arbitrary criteria or largely on political grounds.

Insufficient human capital is another major constraint on local authorities in the developing world that affects their ability to function as effectively as their counterparts in developed countries. A lack of human resources and training lead to poor administrative and managerial capacity, further impeding the service performance of local authorities.

Given the limited resources available in developing countries and the limited capacity of local authorities, it may be desirable to have more central government monitoring and support of local authority activities than would be the case in developed countries. Central government guidance and assistance help to ensure that basic national priorities are not being infringed on by local activities and that scarce resources are not being wasted. There is, however, a delicate balance to be maintained between ensuring that national priorities are being met and protecting as great a degree of local autonomy as possible. This is particularly important given the fragile state of political institutions in many developing countries and the possibility that existing regimes will try to institutionalize their power rather than develop democratic mechanisms.

The political culture in developing countries may be the most significant determinant of how much decentralization actually occurs. The central issue may be how much power the current ruling group is willing to risk sharing with other groups, which may be seen as serious rivals and a threat to the current regime. These other groups may have tribal/ethnic affiliations that differ from the group in power, and may have significant geographical concentrations of strength which could be used to undermine the current government's power base if significant decentralization were allowed to occur. Failure to allow some degree of local self-government, however, may eventually create serious problems for the ruling group.

Revenue System

The basic guidelines for a local revenue system outlined in the fiscal federalism model are very much applicable to developing countries. First, it is desirable to keep the local tax system as neutral as possible. Second, the benefit principle should be followed in the interests of efficiency in resource use, although equity concerns also have an important role to play. Finally, spatial and intergovernmental issues must be taken into consideration.

Despite the relevance of the basic revenue guidelines to developing countries, it is important to recognize that the context in which they are applied will often differ substantially from the developed nations. Revenue options may be more limited due to more extreme environmental, cultural, institutional, and political constraints, and local authorities may be more reliant on central government for collection assistance and/or grants than they are in the developed world. Furthermore, higher levels of government in developing countries control local government revenue systems in many ways, including setting tax rates, stipulating tax exemptions, and directly influencing the size of tax bases. These various problems and constraints can have a serious impact on the structure and operation of local revenue systems. In a study of local government systems in a sample of developing countries, Bahl and Linn (1983) found that few countries exhibit an efficient assignment of local government revenue authority.

Summary of Issues

The above considerations suggest that some aspects of the traditional fiscal decentralization theory are not applicable to developing countries. Although many of the basic principles universally apply, some of the critical assumptions of the model, both explicit and implicit, are significantly violated, and various local conditions affect the way the model should be interpreted. The main areas of concern are as follows:

1. The role of the public sector is often more extensive in developing countries than in the developed countries because private sector institutions are not as well-established. This means that there may often be an expanded role for local authorities.

2. Needs for public services as a production input may differ widely across local authorities because of highly significant spatial differences in economic opportunities and constraints in some developing countries. To the extent that

this heterogeneity of preferences exists, a greater role for local authorities is justified.

3. There are also factors that suggest that preferences in developing countries could be less heterogeneous across local authorities than in the developed countries. Poverty would appear to be a particularly significant constraint on the development of widely varying preferences for public services. Preferences, to the extent the term can be applied, may be largely for a minimum level of basic services rather than for different levels of a wide variety of services. The few major distinctions in preferences may largely be explained on the basis of rural versus urban location and the broad types of economic activity that thrive in different areas. Although these distinctions affect the mix of required services, preferences regarding service level may not differ much across areas with similar economic bases except with respect to required scale.

4. The fiscal federalism theory assumes a high degree of mobility in order that citizens are able to move to an area that provides their preferred mix of local public goods and services. For both cultural and economic reasons, mobility in less-developed countries may be restricted and permanent relocation away from the area of origin may be much more limited than in the developed countries. Also, to the extent that cultural allegiances based on social and ethnic affiliations are more important than individual decisions,

the heterogeneity of preferences across space may be reduced.

5. Even if preferences are more homogeneous across local authorities in developing countries, more highly centralized provision of public services is not necessarily in order. The distance between local authorities and poor systems of roads and transport often generates a degree of geographic inaccessibility that makes regional or central government provision of services difficult. It is also important to ensure that local residents have a degree of local self-government, especially in countries where there is strong tribal affiliation in local areas and particular tribes dominate the national political scene.

6. Unlike in developed countries, local authorities in some developing countries do not always provide a relatively standard set of services nor do they have access to a relatively standard set of revenue sources. As noted earlier, some of these differences in the composition and level of local government revenues and expenditures are due to variations in economic base. Many, however, are imposed by arbitrary and inconsistent central government policies rather than self-selected on the basis of local preferences. Such policies may constrain local authorities in other ways as well.

7. Local authorities in developing countries may have varying combinations of urban and rural residents within their jurisdictions. In some cases, therefore, there are

highly heterogeneous preferences for public services within local authorities, a situation that greatly complicates the provision of local public services.

8. Local authorities in some developing countries are not part of an integrated system of decentralized government and are not properly empowered to provide the services for which they are responsible. Attempts to correct these deficiencies may be frustrated by substantial political, legal, and institutional constraints. In some cases, ruling national political forces may be so powerful and unwilling to share power with rival or minority groups that all attempts to decentralize to any significant degree will be effectively blocked.

9. Local authorities in developing countries are more likely to be plagued by human resource constraints than their counterparts in the developing world. Deficiencies in managerial and technical capacity undermine the ability of local authorities to satisfy the preferences of their constituents. This factor, combined with the need to ensure that the use of scarce resources supports national development priorities, suggests that there may be a need in some developing countries for the central government to play a greater role in monitoring and supporting the activities of local governments. This need, however, can easily be abused by national rulers wishing to consolidate their control.

Relevance of Basic Principles

It is clear from the discussion above that there are certain problems with attempting to apply directly to the developing countries the economic models of local government formulated in the context of the developed world. However, many of the basic principles of these models, as qualified by the special or more serious problems and circumstances of the developing countries, can be used to analyze and evaluate the fiscal role of local government in the developing countries. The following basic principles and issues should be taken into consideration when evaluating the fiscal structure of local government and its relationship to other levels of government in developing countries:

1. The considerations outlined earlier suggest that there are the diversity of environmental conditions in developing countries may make spatial preferences for public goods and services more heterogeneous than in developed countries. At the same time, certain economic and cultural factors may make preferences more homogeneous. These factors must be carefully weighed in determining the appropriate degree of decentralization for the provision of public goods and services.

2. In order to minimize costs and provide services efficiently, it is preferable to assign many public service functions to decentralized levels of government in developing

countries even if preferences are not highly heterogeneous. This is true for a variety of reasons. First, in some developing countries, local authorities are often geographically dispersed and/or not easily accessible. This makes having large jurisdictions more expensive and difficult. Second, services that can be readily provided on a small-scale basis might be more easily managed at a decentralized level and better tailored to the local population. Third, it is desirable to give some sort of control and management power to local people or their elected representatives, especially if they are geographically distant from the people who would otherwise govern them and/or if they belong to an ethnic minority. This may help in building national unity while providing incentives for participation and for the development of managerial and technical skills.

3. Externalities and economies of scale must be taken into consideration in evaluating the assignment of service provision responsibility in developing countries. This is true even in cases where very different types of local government are involved. For example, water is a service that is often provided in both rural and urban areas of developing countries. There may be economies of scale involved in providing this service over a larger area. These could be exploited, for example, by having a regional water authority or a cooperative agreement between a rural local

authority and nearby urban local authorities.

4. Cultural and political constraints need to be weighed when considering the allocation of public functions and the size of decentralized jurisdictions. For example, if there is no real difference on other grounds for service provision over a smaller area or a larger one, then ethnic/tribal considerations may suggest that there would be greater cooperation and harmony as well as lower decision-making costs if the jurisdiction were larger or smaller, depending on the particular pattern of tribal settlement. In many cases, political considerations may be the most important factor in determining the degree of decentralization.

5. Legal and constitutional constraints must be taken into consideration in evaluating the assignment of service functions and tax sources to local authorities. Powers cannot be given to local jurisdictions if they are not allowed to have them under the provisions of the constitution and relevant legislation. If there is an economic rationale for making an assignment that is prohibited, attempts can be made to amend the constitution or legislation. This has been done in a number of developing countries.

6. Resource and managerial/administrative constraints, which are likely to be much more severe and pervasive in developing countries than they are in developed ones, should be taken into account when evaluating the assignment of

functions and revenue sources to levels of government, but they are not by any means the final consideration. Assigning service functions on economic grounds to levels of government that are ill-equipped to handle them makes no sense in the short-run. Redistributive grant schemes and training programs can be designed to help overcome or alleviate deficiencies in these areas over time.

7. The national or local nature of a public service should be evaluated when considering the assignment of service provision responsibility. If a good is directed at purely local priorities, it should be provided at a local level. If it is a service related to national development goals, a case can be made for higher level provision or subsidization, even if the service could be provided locally. This is particularly true when poor local capacity and scarce resources are a major constraint. Furthermore, scarce resources may dictate the need for a national strategy of non-uniform development which concentrates available resources in areas where the benefits generated for the national economy are expected to be greatest.

Framework for Analyzing and Evaluating the Fiscal Role of Local Government in Developing Countries

A framework for analysis and evaluation of a local government fiscal system in a developing country must take into account the general factors and principles discussed above. Major components of a local government system and various issues and factors related to their operation and performance have to be considered both separately and in relation to each other. Some of these are outside of the realm of economics, but can have an important impact on the way the system works or fails to work.[15]

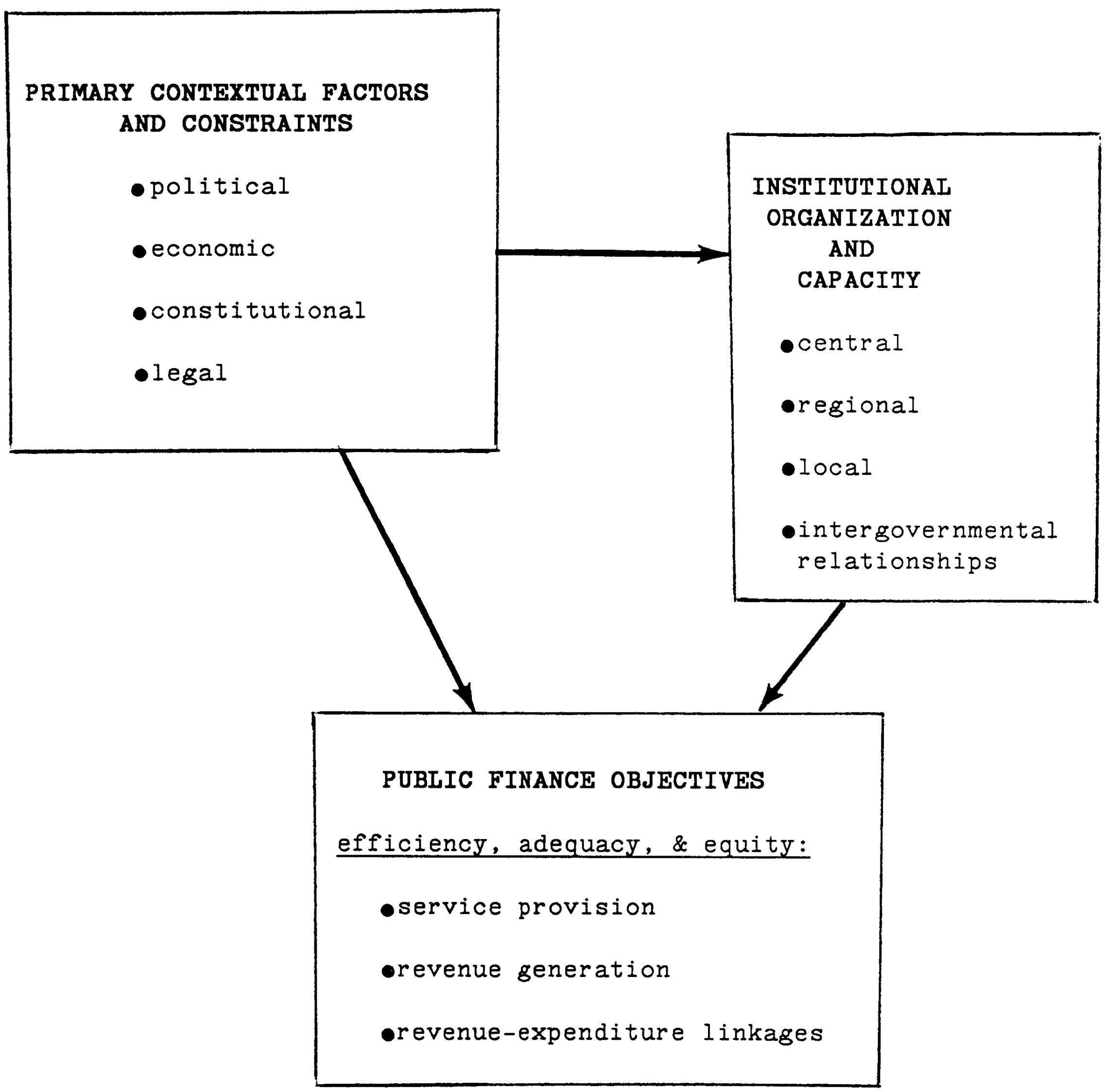
There are several levels of concern that need to be examined in analyzing the fiscal role of local government in developing countries. These have already been discussed in the previous section and are presented schematically in Figure 3.1, which will serve as a basis for discussion throughout the remainder of this thesis. First, there are a set of public finance objectives regarding service provision, revenue generation, and revenue-expenditure linkages. These relate to the ideal or optimal arrangements for providing public goods and services in a given country. Second, there are a set of issues regarding institutional organization and capacity, which affect the ability of the public sector as a whole to provide public services efficiently and equitably. Finally, there are a set of primary contextual areas and constraints--political, economic, constitutional, and legal--that affect both the institutional organization and capacity framework and the public finance objectives.

Because of their high degree of interrelation, these distinctions--public finance objectives, institutional

[15] Many of these factors to be discussed receive various degrees of consideration in Davey (1983); Bahl and Linn (1983); and Bahl, Miner, and Schroeder (1984).

FIGURE 3.1

ANALYZING THE FISCAL ROLE OF LOCAL GOVERNMENT
IN DEVELOPING COUNTRIES



organization/capacity, and context/constraints--are somewhat artificial, particularly between the latter two categories. It is possible, however, to think of institutional organization/capacity as an intermediate step in the provision of public services. Political, economic, constitutional, and legal factors, to a great extent, determine institutional arrangements and capacity. Institutional factors, in turn, directly affect the ability of the public sector to generate revenue and provide public goods and services equitably and efficiently.

Political and economic constraints are probably the most important determinants of how the system of public finance works in a particular developing country. It is difficult or impossible to overcome economic (resource) constraints, at least in the short run. Political context, as has already been emphasized in the previous section, may in many developing countries be the single most important factor in determining the degree of public sector decentralization. Political power can greatly influence or determine, either directly or through changes in the legal and/or constitutional context, the organization of and interrelationships among government institutions, thereby affecting their powers and their ability to meet public service demands. Political power can also determine the policy direction of existing institutions and/or individual decisions made by them.

This section develops a simple framework for analyzing the fiscal role of local government in developing countries. It incorporates the areas discussed above--public finance objectives, institutional organization/capacity, and primary contextual areas and constraints--and explicitly takes account of their interrelatedness. Public finance issues are dealt with first, followed by an examination of issues related to institutional organization/capacity. Discussion of the broader contextual issues and constraints and how they affect the other areas is incorporated directly into the discussion of public finance and institutional issues rather than treated as a separate section. Examples of how these primary constraints affect the operation of the public sector have already been given in previous sections. This section will show how they must be explicitly considered as they relate to public service provision in analyzing and evaluating the fiscal role of local government in developing countries.

Public Finance Objectives

This section defines how public finance principles should be applied to an analysis of the fiscal role of local government in developing countries. Three interrelated issues, service provision, revenue generation, and revenue-expenditure linkages, are covered.

Service Provision

Service provision is the key area involved in analyzing local government because the fundamental purpose of local authorities is to provide services to the people. The basic issue regarding service provision is what services should be provided by local government and for which services is more centralized provision justified. There are also a variety of other considerations related to this basic issue. The following factors must all be taken into account in dealing with service provision:

Need in the area for particular services based on local economic activities and preferences. As discussed earlier, in many developing countries the emphasis will be on providing a minimum level of basic services. The nature of these services, however, will differ among different types of local authorities. For example, in some towns there may be a need and sufficient resources for waterborne sanitation, while in others pit latrines will be adequate. This sort of decision can be made exclusively at the local level unless there are externalities involved. It has also been noted that rural and urban areas have different service needs, and that even different rural areas require different types of services to support different economic activities and lifestyles.

Externality or scale-economy considerations. As already discussed, there are some types of goods and services that can be more efficiently provided over a larger jurisdiction by a higher level of government or jointly by a group of local authorities. The example of water supply has already been given as an example of economies of scale. There are some unusual types of externalities in developing countries that local authorities would be unlikely to pay attention to. For example, livestock that originate in certain areas are not adversely affected by particular types of diseases carried by ticks or other parasites. Because these livestock have a high degree of immunity to the diseases, neither their owners nor the local government will bother to take pest control measures. During the dry season when the animals are moved into other areas in search of water, they may come into contact with other animals that are susceptible to the diseases and place them in life-threatening situations. Some of these diseases can spread like wildfire and kill hundreds of animals in a very short period of time. Thus, a case can be made for providing control measures cooperatively or centrally.

Some local government services must be provided jointly. Certain local government services are highly interdependent, and one must be provided if the other is to be provided. It makes no sense, for example, for an urban local authority to construct a sewerage system or a slaughter house if an adequate water supply does not exist. Similarly, a cattle dip in rural areas will not be usable if there is no water supply in the area.

<u>Local government activities should support/augment private sector activities</u>. It may be necessary for local authorities to provide some services that are provided by the private sector in more developed countries. Examples include markets, slaughterhouses, grain storage facilities, and veterinary services. Any of these could be provided privately, but people in some areas may be too poor or just unwilling to get involved because the expected returns are not high enough and/or because the needed facility involves significant scale economies or externalities.

<u>Services should cover all relevant areas in the local authority's jurisdiction to as great an extent as possible</u>. Residents who demand and are willing-to-pay for public services should be provided with them. Rural-urban distinctions and differences in service requirements within the local authority need to be taken into account for efficiency reasons. There is also an equity dimension here: it may be decided that certain basic services should be provided uniformly or wherever they are needed, regardless of ability-to-pay.

<u>Existing differences in per capita expenditures across local authorities should be justified on some reasonable grounds</u>. Such differences, for example, might reflect intergovernmental differences in preferences, which are related to such factors as economic base and wealth. To the

extent that preferences are the determining factor in interjurisdictional differences, the system is working efficiently. Differences in service provision due to some factors, such as wealth, may be undesirable, but can be influenced by central government programs. Other types of differences, however, may be difficult to justify and to overcome. In some cases, for example, intergovernmental differences in per capita spending may largely reflect arbitrary central government decisions regarding the assignment of service functions and revenue sources.[16]

Central government has a coordinating role to play for certain services. Particular services, even if they are provided to some extent by local or regional authorities, will need to be coordinated by central government. Such services involve significant externalities, whether natural or created through specific national development strategies. A national roads network, for example, will need to be centrally planned or coordinated, even if decentralized governments have an important role to play in financing, constructing, and maintaining parts of it.

In some developing countries, nongovernmental organizations will have a role to play in local service provision. Various types of charities and nonprofit

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[16] Of course, there are problems in using per capita spending as a measure of the level of service provision due to such factors as interjurisdictional differences in costs and quality.

organizations are involved in basic education, health care, veterinary, and agricultural extension and support, and a variety of other services vital to the local communities, particularly in rural areas. These activities should be taken into account when planning the allocation of scarce resources to local services.

<u>Capacity of the local authorities to provide particular services or some plan for developing such capacity</u>. Although there may be a good economic rationale for assigning a particular service to local authorities, there is little sense in doing so if the local authority is not capable of providing it. In such cases, central government staff support may be required, at least until local authority staff can be properly trained to provide the service. In other cases, varying degrees of financial support might be required, perhaps on a continuing basis.

<u>The role of national politics in assigning service functions</u>. In some cases, certain services are assigned to the central government in order to further national goals even if a case can be made for local provision. Education, for example, is not only funded, but sometimes actually provided by the central government in some developing countries. This is probably not for scale reasons, but because the government may use the system to further its own ideology or demonstrate to the people how much the government is doing for them. In such cases, it may be impossible to

argue for the service to be locally provided regardless of what economic considerations may suggest. In extreme cases, the central government may consolidate power by controlling a wide variety of services which could be provided locally.

Revenue Generation

The basic issue in evaluating revenue generation is what sources of revenue are appropriate for local authorities in a particular country. Appropriate revenue sources may well differ across different types of local authorities in a given country. It is also important to understand the effects of the current revenue system and how well it functions. The following considerations are important:

Local revenue sources should be appropriate to the local economic base and local ability-to-pay. Local authorities should have access to a reasonably well-diversified revenue base. This would include some mix of elastic sources of revenue and sources with a fairly stable yield.[17] In many developing countries, central governments have a tendency to reserve the most elastic and most productive revenue sources entirely for themselves. It will be very difficult to build an effective system of local

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[17] The goal of having an elastic revenue base conflicts with the goal of having a stable one. It is possible, however, to diversify the revenue base in such as way to include both stable and elastic sources. Having stable sources will prevent overall revenue from falling too much in bad years, and having elastic sources will ensure that there is growth of the base in good years.

government if this is the case unless local government autonomy can be preserved in a system in which central government essentially funds local authorities.

In the interests of preventing efficiency effects, local government revenues should be derived from most or all economic activities. This could be done either by some type of fairly general tax or a set of taxes that cover different types of economic bases. There may be an equity reason or some other justification to exclude certain activities from taxation, but this may erode the tax base, a situation which few local authorities in developing countries can afford, and it might generate undesirable efficiency effects.

The revenue structure should not provide perverse incentives for private decision-makers. This is just a standard warning to be aware of the efficiency effects of taxation. It was argued earlier that mobility may not be as great a problem in developing countries as it is in the developed world.[18] Poorly devised taxes, however, can still generate undesired results. For example, a progressive rate structure for an agricultural land tax might encourage land subdivision, which could lead to less productive methods of

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[18] There is a possibility that certain types of mobility may be more important in some developing countries. When there are a few instances of large-scale domestic or foreign-supported investment projects, the chosen location may well depend on preferential tax treatment by central and/or local government. This type of situation may generate very significant consequences for the location and allocation of resources, much more so than when many investment projects are occurring over a large area.

cultivation and lower crop yields. These types of effects must be carefully avoided for economic reasons, although subdivision for the purpose of land redistribution may be a political goal in some developing countries.

Entrepreneurial revenue-raising activities should be exploited by local authorities in developing countries. As noted in the section on service provision, local authorities in developing countries may be called upon to provide some services that would be provided by the private sector in more developed countries. The provision of these services may have the side benefit of generating substantial income for the local authorities. This is perfectly acceptable if the charges for the various services are reasonable. The additional revenue could be used by the local authorities to provide infrastructure and services that generate further local economic growth and improve the well-being of local residents.

Self-help activities should be encouraged in areas where it is possible to do so. As noted earlier, in some developing countries, especially in Africa, the self-help ethic is culturally pervasive. Local people contribute money to the building and maintenance of school and health facilities in addition to paying their regular taxes. They also save the local governments some expenses by donating materials and labor. This can be an important part of service provision in some areas.

Particular groups within a local authority might be taxed more heavily than others for both equity and efficiency purposes. The incentive problems noted above must, of course, be avoided as much as possible. However, there is room for some redistribution at the local level in developing countries through the process of raising more taxes from higher income people to provide services that are enjoyed by the general population. There is also a simple benefit issue involved here. In some areas, wealthier people use a higher level of services than the poorer people, and they should be made to pay for them.

The local government tax system should exhibit as much equity as possible. The case has already been made for some degree of progressivity where possible, but the system, at the very least, should be proportional in the interests of vertical equity. Horizontal equity should also be respected to as great an extent as possible. It is difficult, for example, to justify taxing income from food crops at a higher rate than income from cash crops unless there is a very good reason to affect the composition of agricultural production. Finally, there should be geographical equity. People in one part of a local authority should not pay different rates on the same taxes solely by virtue of differences in where they live or work. Such differential treatment may be justified, however, if economic base and incomes vary widely across different areas in particular local authorities.

Political, constitutional and legal constraints, as well as deficiencies in administrative capacity, must be considered when designing a local tax system. Many examples of these constraints have already been given in this chapter. Some of them can be overcome with time if the central government is willing to work towards that goal. Others, particularly those related to political considerations, may be more difficult to deal with.

Revenue-Expenditure Linkage

The local government system must be set up in such a way that there is a proper correspondence between service responsibilities and revenue availability. The following considerations should be weighed:

There should be consistent and defensible guidelines for setting all tax rates and fees charged by local authorities. In many developing countries, tax rates, license fees, service fees and other types of taxes are set arbitrarily or entirely on the basis of political favoritism. Instead, there must be some rational and equitable basis devised for doing this, and it should be consistently applied.

Services that can be provided on a fee-for-service basis should be self-financing to as great an extent as possible for efficiency reasons. Those who benefit from a service should generally be required to pay for it. Of course, there may be some legitimate reasons for subsidization, such as the existence of externalities, support of a particular growth strategy, or redistribution. Some rural local authorities in developing countries, for example, are in the business of providing veterinary services, such as livestock dipping to protect herds against disease-carrying ticks. If the dipping fee is too high, owners may refuse to dip their livestock, and a serious and economically costly epidemic could result.

General fund taxes (land rates, trading license fees, etc.) should be set at a rate sufficient to cover costs of services that are not self-financing. The arbitrary methods of setting these rates in some developing countries means that even if local authorities were to collect all of the income due to them, they would still be unable to balance their budgets. Of course, some local authorities do not have the fiscal capacity to provide their services without taxing at an unreasonably high rate. In such cases, it is the responsibility of the central government to step in and offer whatever assistance it can.

There should be some mechanism for recovery of costs for services provided to residents of other jurisdictions. The difficulties of applying the benefit principle in a spatial context, in which residents of different jurisdictions interact substantially, mean that residents of one jurisdiction may use the services of another jurisdiction on a regular basis without paying for them. Various mechanisms can be used to ensure that the benefit principle is more closely followed, including various types of fees and taxes that accrue to non-resident users of local services and subsidization by more centralized levels of government.

Central government transfers may be required for some poor local authorities or to subsidize certain services. It is understood that many developing countries are too poor to be able to provide central services fully much less significantly fund local authorities, but there is usually some role the central government can play in financially assisting local government. Transfers may take the form of revenue sharing from the central government general fund or locally assigned shares in particular central government taxes. In addition, categorical grants can be used to subsidize priority local public services that generate positive externalities and/or improve equity.

Institutional Organization and Capacity

The organization of local and central government institutions, the ways in which they interact, and their technical and managerial capacity are determined by the political, economic, constitutional, and legal context in a particular country. Institutional organization and capacity have a significant impact on the ability of the public sector to provide public services for which there is a demand.

Institutional Organization Issues

The institutional procedures and relationships that exist among different levels of government have an important impact on the way the overall government system performs. The following issues in this area need to be taken into consideration when evaluating the fiscal role of local government in developing countries:

Mechanisms for local intergovernmental cooperation may have to be developed. As already noted, in cases where demand is invariant across wide areas, or where significant economies of scale or externalities exist, it would be more efficient to provide services through formal intergovernmental cooperation if a higher level of government is not going to step in. Regulations and mechanisms should be devised to permit the organization and operation of such cooperative efforts. Provisions could also be made for creating separate regional authorities to take responsibility for particular services.

Some support services and supervision of local authorities by the central government may be necessary. Supervision may be particularly important in developing countries where local capacity is inadequate and bribes and corruption may be a way of life. Such supervision may help local authorities to discharge their responsibilities more efficiently and insure that national development goals and strategies are being met by the local authorities. Planning and technical support from the central government may also be necessary because of a lack of engineers, architects, accountants, and other skilled personnel in local authorities. There is a delicate balance to be maintained in order to prevent overinterference and overcontrol by the central government from actually impairing efficiency, perhaps while attempting to improve it. Also, it is important to ensure that central government institutions that monitor and support local authorities are properly empowered, staffed, and organized, and that their operating procedures are consistent and efficient.

<u>There is a need for effective intergovernmental coordination of development activities in developing countries</u>. A complex multi-tiered public administration system was installed by colonial powers and still exists in many developing countries, and redundancy in service provision responsibility as a means to achieving national development objectives is not uncommon or necessarily undesirable. In order for such a system to work effectively, however, there must be coordination of the activities of local authorities, central government ministries, provincial, regional and district administration, parastatals, non-governmental organizations, and other agencies and organizations involved in various types of public service provision in developing countries.

There is likely to be a need for central government support of local authority capital spending. In many cases, local authorities in developing countries do not have the resources to build the type of basic infrastructure that encourages economic growth. Many local authorities do not have access to private credit markets because they are forbidden it by law, cannot afford to pay commercial interest rates, or are not considered to be worthy of credit by the lending institutions. If capital projects are to be financed, the central government will have to provide access to credit on some terms the local authorities can afford, or will have to share responsibility for the planning and of local authority infrastructure. The problem of existing local authority debt may have to be dealt with in many developing countries before additional loans can be made.

Local Administrative Capacity and Procedures

The preceding discussion focused on what the central government should do to support local authorities. This section deals with the major capacity and procedural problems of local authorities, some of which can be alleviated primarily through local action, while others require more central government assistance. In developing countries, a lack of skilled labor and efficient operating procedures can cripple even properly empowered local authorities. These considerations will affect the financial position of local authorities, their ability to provide the services and collect the revenues they are supposed to, and the types of central government interventions and supervision required to ensure that local authorities operate as effectively as possible. The following points merit attention in assessing local administrative capacity and procedures:

<u>Local authority operating procedures should be appropriate to the types of responsibilities the local authorities have and the level of expertise available</u>. Many developing countries adopted the accounting, recordkeeping, and financial management systems of their colonizers. Some of these procedures are unnecessarily complex and cumbersome, and they are beyond the capacity of local authority officials to manage properly. In general, administrative and operating systems and procedures used by local authorities should be simple and basic, requiring a minimum level of skills and a minimum effort to use. Such procedures should also be standardized, and all employees who use them should be trained properly.

<u>Local authorities should institute methods of cross-checking records whenever financial transactions and disbursements of materials are involved</u>. Given the institutionalized nature and cultural acceptance of corruption and bribe-taking in some developing countries, there must be procedures for handling financial transactions and inventory control to ensure that records can be cross-

checked by several independent officers. Corruption is a major drain on local authority funds in some countries, and the financial position of some local authorities could be greatly improved if it were controlled to a greater extent through local and/or central government action.

Local authorities should use incentives whenever possible to encourage better performance by employees. Public administration systems in developing countries are notorious for poor pay and poor incentives, which may lead to some of the inertia, corruption, and inefficiency they often display. The use of such incentives as bonuses, pay raises, and assignment of greater responsibility and promotions as a reward for job performance may help to improve overall revenue collection and service provision in some developing countries.

Conclusion

No framework for evaluating the fiscal role of local government in developing countries is going to be able to take full account of all of the factors that affect the role and operation of local government. Indeed, part of the point of this thesis is to demonstrate the great diversity across local government systems in developing countries along many dimensions that affect the optimal assignment of public service responsibility among levels of government. The guidelines outlined above touch on many of the important issues, but critically examining real world cases in detail will certainly reveal many additional considerations.

All of the factors discussed in the above guidelines are affected by cultural, legal, political, and institutional constraints that may strongly affect the possibilities for the evaluative criteria to be met. Many examples of how these various constraints operate have already been mentioned or discussed, but a researcher will always have to be alert for others that exist in particular cases. In some countries, these constraints may be open to change over time. In other cases, they may be fairly rigid or completely insurmountable. The emphasis must be on attaining the best system of local government that is possible over some reasonable time frame given existing conditions. More substantial reforms may be implementable as greater development occurs over the longer term.

The following chapters turn to an examination of the case study country, the Republic of Kenya. The framework explained above, along with the analysis of important historical factors to be discussed in Chapter 4 and contextual factors which came to light during the fieldwork conducted for this research, will be used to analyze the system of local government in Kenya in Chapters 5, 6 and 7. In the process of conducting the analysis and evaluation of Kenya, it will be possible to illustrate and to clarify further the importance of context in the process of defining an appropriate fiscal role for local goverr ent in developing countries.

CHAPTER 4

HISTORY, DEVELOPMENT, AND CURRENT STRUCTURE OF LOCAL GOVERNMENT IN KENYA[1]

This chapter begins by tracing the history and development of local government in Kenya. This exercise provides a background for understanding the way in which local government currently functions, and it also provides some insights into the possibilities for local authority reform. After examining its history and development, the present structure of local government in Kenya is described in detail as a prelude to evaluating it.

Most local government systems in Africa were developed during colonial rule earlier in this century. Local governments were set up in the pre-independence period both as a means to impose colonial control and to educate the native people in the ways of the colonial powers. Early colonial administrations were often highly centralized under powerful colonial governors. Decentralized institutions began to emerge only after European settlement began to spread and substantial development had already taken place, and only under pressure from settlers groups and African nationalist movements.

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[1] This chapter is based largely on the following sources: Akivaga, Kulundu-Bitonye and Opi (1984); Hicks (1961); Huxley (1935); Kaplan, et. al. (1976); Oyugi (1983); various Government of Kenya reports and laws; and, numerous interviews with present and former Kenyan officials.

In the British colonies in Africa, some type of local institutions were set up almost from the beginning of colonization, but most of these had few powers and resources. There had traditionally been a dichotomy between local governing institutions for the indigenous peoples and those for the settlers. In Kenya, the local government institutions for the natives were established prior to those for the settlers. This is probably the case because in the early years there were few settlers, and they were largely concentrated in high potential areas where their needs could be attended to by a central administration.

The two-tier settler/native system of local government existed in most cases right up to independence, which for most African nations occurred after 1960. In the post-independence period, a number of important changes developed as African nations struggled to find their own identity and come to terms with their own culture and the western systems and ideas that had been introduced to them during the colonial era. The history and development of local government in Kenya very much follows the pattern briefly described above.

Local Government in the Colonial Era

Because the settler and native forms of local government developed differently, it is appropriate to consider them separately before discussing how they were merged into a single system after independence.

Native Local Government

Colonialist-designed native local government in Kenya began, at least in name, just prior to the turn of the century. The East African Order in Council was passed in 1897 to create councils called "native courts" among the tribes. The function of these courts, however, was not clearly specified, and they in fact had little authority. The British had set up a provincial administration in Kenya, and the function of these courts was only to have some sort of official status for the African representatives who dealt with the provincial commissioners.

In 1902, the Village Headman Ordinance was passed. This law gave the provincial commissioner the authority to name natives of his choice to be official headmen of villages or groups of villages. The stated duties of these headmen were to maintain law and order, to help the provincial commissioner collect taxes, to maintain local roads, and to assist as arbitrators in minor African disputes and legal cases. The Townships Ordinance of 1903 provided for local government under the provincial commissioners in urban areas, with Nairobi and Mombasa the first settlements to be granted township status.

Creating the position of headman was an attempt by the British to set up an authority structure, based on trusted locals who would help to protect settler interests and cooperate with the colonial administration. In fact, the concept of chief or headman was somewhat alien to many Kenyan tribes, which were traditionally governed by councils of elders rather than individuals; nevertheless, the Village Headsman Ordinance formed the basis for the colonial system of administration in Kenya, known as the "Native Authority System." This system, based on direct interaction between the colonial administration and a strong native chief acting as the head of a local council, was formally enacted and detailed in the Local Authority Ordinance of 1912.

Following the passage of this ordinance, there were attempts to establish provincial level councils that incorporated both settlers and natives. There was strong opposition to this concept from many settlers who preferred to have separate institutions for the natives. There was also a great deal of controversy about how these provincial councils were to be selected, what their composition would be, and what responsibilities would be assigned to them. In the end, it proved to be impossible to come to an agreement on these issues, and the idea of integrated provincial councils was dropped.

World War I brought a new era of local government to East Africa. In the years following the war, there was an additional surge of British interest in the area, and Kenya was officially transformed from the East African Protectorate to the Kenyan Colony. Kenyans who had fought in the war returned to their villages with a new view of the world and greatly expanded horizons. A number of native organizations were formed, usually along tribal lines, and these later became the basis for the nationalist movement in Kenya. The growing political awareness of the Africans and the expanding interests of the British colonialists necessitated that changes be made in the way the colony was governed.

The Kenya Legislative Council passed the Native Councils Ordinance in 1924. This legislation established Local Native Councils (LNCs) in the districts, which were administrative subdivisions of the British provinces. These bodies were composed of the district commissioner, the assistant district commissioner, native chiefs (headmen) and other Africans appointed at the discretion of the provincial commissioner. Thus, it was essentially a native organization, which had colonial representation by the two principal British administrators in the district. However, all of the African members of the LNC were directly appointed by the colonial administration.

The LNCs were given substantial responsibilities relative to those enjoyed by earlier native councils. Their powers included the ability to pass resolutions, enabling them to collect the local native rate, a district tax on Africans. This power was given well before the settlers were allowed to levy their own local taxes. They were also responsible for certain important service functions, including the provision, maintenance, and regulation of water and food supplies; the regulation and use of forest, agricultural, and pastoral lands; the provision of markets and slaughter houses and the collection of market fees; and the provision and regulation of services in the areas of education, roads and bridges, sanitation (latrines), and agriculture and livestock. Any resolutions passed by the LNCs, however, were subject to the approval of the provincial commissioner and the governor of the colony.

The role of the LNCs was sharply criticized by Kenyan nationalist leaders. It was felt that these councils were basically a useless showpiece devised by the colonial authorities to make the Africans think they were gaining control of their own affairs. The LNCs became extremely unpopular in some areas because they were perceived as using African leaders to force colonial policies on the African people. Under pressure from nationalist groups, some changes slowly occurred in the LNCs over a period of several decades. In 1937, for example, a new Native Authority Ordinance was enacted allowing some councillors to be elected by the people to the district LNCs, although the district commissioner could still remove any elected councillor he perceived to be inappropriate.

The nationalist leaders were never satisfied with the structure of the LNCs even after they were reformed. Oginga

Odinga, a Luo leader and early LNC member who later became the country's first vice-president, sharply attacked the LNCs:

> Matters already decided and finalized by the government were brought to the councils for confirmation and acceptance. Council members were powerless to change anything or to make suggestions contrary to the decisions already made...Measures which were unpopular were imposed through the councils, punishments for infringements of unpopular measures meted out through us, and the government told the people: you elected your representatives to the district councils, this is their decision [Odinga (1967), p. 92].

Despite the lack of autonomy of the LNCs and the fact that they provided only limited services, they were an important step towards some degree of self-government by the Africans. After many years of struggle between the colonial administration and the Kenyan nationalists, and in response to a strong directive from the British Colonial Secretary, proposals were made to redefine and restructure the LNCs in the 1940s. After further debate and struggle, the Local Government Ordinance was finally enacted in 1950. This legislation established the African District Councils (ADCs) to replace the LNCs.

The African District Councils were not dramatically different from the LNCs in terms of their level of autonomous power, but there were a few important distinctions. First, the majority of ADC councillors were elected, although the method of choosing the chairman of the council was left to the discretion of the district commissioner. Second, the ADCs were given formal legal status: they could sue and be sued, and they could enter into legal contracts. Third, they were given the authority to appoint administrative staff and to set up committees to deal with specific functions, much like present-day local authorities. Fourth, the ADCs were given the authority to form joint committees with neighboring councils to undertake joint projects of mutual interest and benefit. Fifth, divisional and locational (subdivisions of districts) councils were formally established as grassroots advisory bodies to the ADCs. Finally, a system of central government grants was begun with the establishment of a 50 percent grant for approved expenditures on health services.

ADCs did not become fully functional for some time after they were legally allowed to be established. Soon after the passage of the Local Government Ordinance in 1950, some elements of the nationalist movement in Kenya turned to violence, and the so-called "Mau Mau Emergency" ensued. This crisis, which ultimately led to Kenyan independence, prevented ADC elections from being held until 1958. The ADCs were the last colonial form of native local government in Kenya. After independence was achieved in 1963, the ADCs were blended into the white settler system of local government, which is explained below.

Settler Local Government

There was no formal local government institution for settlers in Kenya during the early years of colonization, but settler associations were formed from around the turn of the century. The Farmers and Planters Association was founded in January 1903 under the leadership of Hugh Cholmondeley, Lord Delamere, a leading spokesperson for the settlers until his death in 1931. The association had 23 members, and its primary purpose was to find a market for potatoes. As settlement grew, its membership increased rapidly, and its purposes broadened. In 1904, it was renamed the Colonists' Association and welcomed all European settlers who wished to join. The new organization was designed to protect the interests of the settlers and to encourage additional settlement by Europeans.

The Colonists' Association was the only major grassroots organization representing the settlers until the outbreak of World War I. In 1915, the Registration of Persons Ordinance established District War Committees (DWCs) to deal with local wartime problems and to manage the estates of Europeans who were away at war. Rather than dismantle the DWCs after the war, the administration reorganized them into District Advisory Committees (DACs) in 1919. These DACs operated only in districts in the white settler areas, the so-called "white highlands." They were primarily designed as a way to organize settlers at the district level and formalize their relationship with the colonial administration in order to protect their interests, although they had a few official service functions, such as road maintenance.

The settlers, however, were not satisfied with the structure and responsibilities of the DACs. In response to pressure from the settlers, the Governor of Kenya appointed a Local Government Commission under R.H. Feetham to examine the structure and functioning of local government in Kenya in 1926. The Commission recommended keeping separate institutions for the natives and the settlers and strengthening the settler councils. It further recommended that elected district councils with full executive authority be formed in the seven major settler areas. These semi-autonomous councils would govern the rural areas in the districts. Townships and municipalities would remain under the administration of the district commissioner but would have their own advisory committees.

In response to the Commission Report, the Legislative Assembly passed the District Councils Ordinance in 1928. The new district councils replaced the DACs in the European settler areas. Membership on the council was through election by fellow Europeans, although there was a provision made for membership of Asians. No native Africans could vote for candidates or serve on the district councils, even if they lived in the white settler districts.

Nationalist movements in African countries and greater awareness of the situation in the colonies at home began to exert pressure on the British Government to reform the colonial administrations during the 1940s. It was becoming evident that the colonies would eventually have to be granted more, or perhaps total independence, and the British wanted to ensure that the type of governments that would be set up would be friendly and familiar. In 1947, the British Colonial Secretary, Lord Creech Jones, issued a Local Government Dispatch calling for a systematic introduction of the Westminster type of local government in all British colonies. This was seen as the first step of a programme to set up systems of national self-government over time. The Colonial Secretary stated in this Dispatch:

> Since I took office in October, I have been considering some of the basic problems of African administration; I think that it is right that I should now address you on this subject, since our success in handling these problems, and the extent to which we can secure the active co-operation of the Africans themselves, may well determine the measure of our achievement in the programmes of political, social and economic advancement on which we have now embarked. I believe that the key to success lies in the development of an efficient, democratic system of local government. I wish to emphasize the words efficient, democratic and local. I do not do so because they import any new conception into African administration.; indeed, these have been the aims of our policies for many years. I use these words because they seem to me to contain the whole kernel of the matter: local because the system of government must be close to the common people and their problems; efficient because it must be capable of managing the local services in a way which will help to raise the standard of living; and democratic because it must not only find a place for the growing class of educated men, but at the same time command the respect and support of the mass of the people. ... In urban areas the special problem arises of developing municipal government, or in some places, associating African with non-African communities in municipal government where it already exists. In rural areas local government bodies may be native authorities, large or small, or local native councils as in Kenya. Where native authorities are large and responsible for hundreds of thousands or even millions of people, the

problem is building up a system of local government below them in close touch with the people themselves; where they are too small to be effective, the problem is one of securing fusion or a federation of existing units. The general policy must be applied differently in different areas; the broad aim of securing an efficient and democratic system of local government, will, however, be the same everywhere. ...The problem is fully recognized by the African Governments and is being met in some Territories by the establishment of regional or provincial councils, through which a chain of representation from the people to the Legislative Councils can be secured. The Native Authorities, as the organs of local government, are the most important link in this chain."[2]

The Dispatch has been interpreted as advocating the institution in the colonies of what might be called the classic British model of local government as set forth by Headley Marshall, Ursula Hicks and Henry Maddick [Mawhood (1987)]. This model presupposes the existence of a local body that is constitutionally separate from government and has responsibility for a significant range of services. This body should have its own treasury, a separate budget and accounts, and the power to raise a substantial portion of its revenue. It should also have a staff under its own control, with decision-making on policies and internal procedure in the hands of a democratically-elected council. Finally, the central government should have no direct role within the local authority, with its agents serving at most in an advisory or regulatory capacity.

2 Portions of Creech Jones Dispatch are quoted in both Hicks (1961) and Akivaga, Kulundu-Bitonye and Opi (1984). This quote has been assembled from material in both of these sources.

The response of the Governor of Kenya to the Dispatch was relatively prompt and clear. The establishment of the African District Councils in the native areas in 1950 was one result of the Dispatch and has already been described. In addition, a new system of local government based directly on the British system was initiated in the white settlers area by the County Councils Ordinance of 1952. The primary unit of local government was the county council, which generally covered several of the district councils, which were left intact. The county councils had primary responsibility for raising revenues and were the only councils allowed to charge land rates. District councils and urban councils were below the county councils, but remained fairly autonomous with respect to their service responsibilities. There were also further area subdivisions called local councils and area councils, but these had little independent power.

The system of different local government institutions in the settler and native areas remained in effect until independence. The Mau Mau Emergency hastened the push for independence and strengthened the Kenyan nationalist movement. Kenya's independence constitutional conferences began with the Lancaster House Conference in 1960, which established the Macleod Constitution and provided for the election of an African majority in the Legislative Council. The role and organization of local authorities became one of the key issues for both the British and the Kenyans at this conference. Soon afterwards, the Kenyan Legislative Council issued Sessional Paper No. 2 of 1961, "The Reconstruction of Local Authorities". This document was the basis for the Draft Local Government Bill of 1962, which outlined the organization of local government.

The Local Government Regulations passed in 1963 removed the two-tier system of local government that had existed between the settler and native areas. The African District Councils were abolished and replaced by the county council system that had been introduced into the settler areas in 1952. Area councils and urban councils were placed under the jurisdiction of county councils, and municipalities and townships were given full autonomy. All of the councils were given significant responsibilities and revenue-raising powers. Local authorities basically operated under the 1963 Local Government Regulations and subsequent minor amendments until the Local Government Act, Chapter 265 of the Laws of Kenya, was passed by the National Assembly in 1977.

Local Government and the Kenyan Constitution

Although the basic role to be assigned to local authorities was decided in earlier meetings in the United Kingdom to draw up a Constitutionfor an independent Kenya, the overall degree of centralization and the structure of the new government continued to be hotly debated in later pre-independence meetings. Two Kenyan nationalist associations dominated these meetings and were at the heart of the debate. The Kenya African National Union (KANU), under the leadership of Jomo Kenyatta, Tom Mboya, Oginga Odinga, and James Gichuru, was a coalition of the two dominant tribes in Kenya, the Kikuyu and the Luo, with a sizeable allegiance from the Kamba. The Kenya African Democratic Union (KADU), led by Ronald Ngala, Masinde Muliro, and Daniel arap Moi, was a defensive coalition of smaller ethnic groups who sought to protect themselves against domination by the majority tribes. The coalition included Kalenjin, Maasai, Luhya, Somali, some Kamba, and several coastal groups, including the Mijikenda.

KANU, under Kenyatta's strong leadership, favored a powerful central government under the banner of national unity. KADU, on the other hand, favored regional autonomy in a federal system with a fairly weak central government.[3] Because of a substantial degree of tribal homogeneity within regions, the KADU leaders felt that this type of system would prevent domination of minorities by the majority tribes. The KADU position was supported by the New Kenya Party (NKP), a union of white settlers, and the Kenya Indian Congress (KIC). Both of these parties obviously represented additional minorities in the Kenyan population.

The Constitutional Conference to design the framework of the new constitution was held in London in 1962. The

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[3] It is important to note that the KADU position focused on the establishment of strong regional, i.e., provincial, rather than local government.

surprise result was a victory for the regionalism supported by the minority party, KADU. This is said to have occurred for at least three reasons. First, the KADU delegation to the conference was persuasive, persistent, and intransigent on the issue of regional autonomy. Second, the KADU plan for strong regionalism won the support of the British Colonial Secretary. Finally, Kenyatta may have feared that independence would be delayed if KANU put up a fight over the centralization issue.

The Framework Constitution adopted in 1962 rejected a truly federal system, but it did give strong constitutional powers to the regions. After the Constitutional Conference, the Kenyans returned to Nairobi and formed an interim KANU/KADU coalition government to work out further details of the new constitution until elections were held in May 1963. Constituency boundaries were drawn up for the new regions basically to coincide with the provinces that had been formed under the colonial administration. These boundaries and election rules somewhat favored KADU by giving greater representation to less populated rural and pastoral areas where regionalism was supported. The Kikuyu and Luo of KANU, although dominant ethnic groups, lived largely in smaller, densely populated areas around Mt. Kenya and Lake Victoria.

Elections were held in May 1963 for both national and regional assemblies. KANU overwhelmingly won the National Assembly, gaining 70 seats compared to 32 for KADU and 8 for a minor dissenting group, the African People's Party (APP). The regional elections were evenly divided along tribal/territorial allegiances to the two major parties; KANU won in Nyanza, Central, and Eastern Provinces, while KADU took the elections in Western, Rift Valley, and Coast Provinces. No regional elections were held in Northeastern Province because of dissent by the dominant Somali tribe.

In the wake of the elections, Kenya was granted self-government in internal affairs on June 1, 1963 (Madaraka Day). Despite the convincing victory of the KANU, the Independence Constitution promoting regionalism was formally adopted by a final Constitutional Conference in September 1983. This constitution is popularly known in Kenya as the Majimbo Constitution.[4] It followed the principles laid out in the Framework Constitution of the previous year, granting substantial power and autonomy to the regional governments. Each region was to have an elected assembly with both legislative and executive powers, the latter being handled by committees. Their powers included control over matters concerning education, health, agriculture, livestock, part of the police forces, and local government. The national administration was also further decentralized and new titles were given to provincial and district administration officers. Provincial commissioners were to be called civil

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[4] Majimbo is the swahili word for province, region, or district.

secretaries, and district commissioners were to be known as regional government agents.

The implications of the Majimbo Constitution for local government were substantial. Local governments, as was discussed in more detail earlier, had long existed in Kenya with certain types of independent powers. In practice, however, provincial and district commissioners, as representatives of the centralized colonial administration, had a great deal of influence on the behavior and performance of local authorities. Under the new constitution, however, local governments were to be entirely under the jurisdiction of the regional assemblies. This had the potential to reduce dramatically the influence of the central government on local authorities as well as lead to different roles and different organization of local authorities in different regions. The Majimbo Constitution mandated a system of government that was far more decentralized than its colonial predecessor.

On December 12, 1963, shortly after the formal adoption of the Majimbo Constitution, Kenya was granted independence (Uhuru). The new government retained the Queen of England as head of state, represented in Kenya by a governor general. The head of government was the Prime Minister (Kenyatta), and there was a bicameral National Assembly. Another important aspect of the new Kenya was the powerful regional assemblies discussed above, which took over approximately one-third of the functions previously controlled by the colonial central government.

Unfortunately, it will never be possible to know if a decentralized Kenya would have been successful. Largely because of a lack of experienced personnel, inefficient planning, and the strong opposition of KANU, the regional assemblies ran into serious problems right from the start. In August of 1964, the Kenyatta government forcefully criticized the regional assemblies and announced its intention to amend the Majimbo Constitution. The desired changes included making the country a republic, unifying the positions of head of state and head of government under an office of the president, and abolishing the regional assemblies. Kenyatta threatened to hold a national referendum on the issue if the National Assembly would not agree to his constitutional amendments.

The Majimbo Constitution had been written to make amending it a very difficult process. However, KADU and other opposition groups were unable to put up much of a fight. In November 1964, the constitutional amendments proposed by Kenyatta were overwhelmingly adopted by the National Assembly. The new constitution, known as the Republican Constitution, came into effect on Jamhuri Day, December 12, 1964, the first anniversary of Kenyan independence. The Queen was removed as head of state, the office of prime minister and the regional assemblies were abolished, and Jomo Kenyatta soon became the first president of the Republic of Kenya. The offices of provincial commissioner and district commissioner were re-established and placed under the Office of the President. In addition, responsibility for police, education, health, agriculture, livestock, land acquisition, local government, and some other services was returned to the central government. Some of these services were quickly reassigned to local authorities, but this was done by administrative or legislative, rather than constitutional, authority. Some additional constitutional amendments occurred in later years, but the centralized system imposed by the Republican Constitution still stands in Kenya today.

Post-Independence Local Government Reform

The role of local authorities in Kenya has undergone some important changes in the period since independence was attained in 1963. The desire of KANU for a strong central government has already been discussed, as has their successful effort to reform the Majimbo Constitution. Although the Kenyatta government was able to eliminate regional government, the local authorities were left with fairly strong local powers. The Kenyatta government continued to consolidate its own power during the 1960s, and there were strong political interests that wanted to limit or eliminate the broad powers of local authorities. The real reason for this desire was primarily to consolidate further political power in the hands of dominant ethnic groups and to keep the power of "troublemakers" from minority tribes in the districts at a minimum. Powerful county council leaders who favorably impressed the local people might have ambitions to Parliament and ideas that conflicted with KANU ideology.

The stated reasons for wanting to limit local authorities were substantially different. Throughout the 1960s, it became fairly easy to criticize the idea of retaining local authorities with significant responsibilities. This was true for several key reasons. First, national leaders could point to the divisive problem of tribalism and the instability that it could potentially lead to. Thus, they reasoned that there was a need for national unity, which to them meant greater centralization under their leadership. Second, although the performance of local authorities was satisfactory in some of the wealthier areas, there were serious problems in many districts, particularly in the more remote rural areas. National leaders were able to point to the financial and managerial problems of local authorities as a reason for limiting their responsibilities. To exacerbate the problem, population growth and demand for some services, particularly education, were growing rapidly during the 1960s. The national politicians observed that local authorities having financial and managerial problems were going to be in even worse shape as demands on their limited capacity grew. Finally, there was a common perception among development experts at the time that centralized administration and strong national planning led to more efficient allocation and distribution of resources, in turn leading to more rapid growth and development. In the view of Kenya's leaders, an overly prominent role for local government could undermine this process.

In 1966, a Local Government Commission was set up by President Kenyatta under W.S. Hardacre to look into the types of reforms that would be necessary to make the local government system in Kenya more viable. The Commission called for sweeping reforms and a general strengthening of Kenya's local authorities. In response to the Commission's report, the Government issued Sessional Paper No. 12 of 1967, which accepted most of the recommendations of the Commission about revitalizing local authorities. The Sessional Paper also indicated the Government's willingness to provide the local authorities with both reliable revenue sources and central government grants. The political will to implement these reforms, however, was not there.

After much debate on the subject, the Government passed the Transfer of Functions Act in 1969. Instead of revitalizing local authorities, this legislation provided for the transfer of several major services, including primary education, health services, and road maintenance, from the local authorities to the central government as of January 1, 1970, except in the seven largest municipalities. This legislation also transferred the Graduated Personal Tax (GPT), a local payroll levy, to the central government, and abolished general grant revenues to the local authorities.

The GPT had been the principal source of revenue for all local authorities. When it was suddenly transferred to the central government along with significant service responsibilities, most local authorities were left in a greatly weakened position. The local authority system itself was left intact, but many of the councils were left with little to do. The stated intent was that this transfer of functions and revenue sources would be temporary. There was to be a complete reorganization, restructuring, and strengthening of local authorities, and service responsibilities, and revenue sources were then to be returned to them. This has never happened.

The major municipalities were least affected by the Transfer of Functions Act. The GPT transfer was accomplished gradually for the large municipal councils, and they retained their major service functions. When the transfer of GPT was completed in 1974, it was replaced with a compensating grant that was also gradually reduced over time. The compensating grant was finally abolished in 1978, but the Government introduced various grants to subsidize the large municipal councils for certain costs incurred in the provision of primary education and health care. All of these grants, except grants for teachers salaries, were abolished in fiscal year 1984/85, placing an additional financial burden on the largest municipalities. No other financial assistance for recurrent expenditure is given to Kenyan local authorities by the central government except limited grants to needy councils, which will be discussed later.

During the 1970s, the need to strengthen local authorities was regularly highlighted by National Development Plans, various special commission reports, and an International Monetary Fund report commissioned by the Government of Kenya.[5] Little has been done to implement any of the major recommendations proposed by these documents for strengthening local government in Kenya. The coup d'etat attempt in 1982 seems to have created additional resolve on the part of the ruling party to consolidate power at the central level.

Relevance of Historical Factors

The history and development of local government in Kenya provides some useful insights into the possibilities for strengthening local government in Kenya today. Several factors stand out as important. First, in contrast to many

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[5] See, for example: The Report of the Public Service Structure and Remuneration Commission, 1970-71; The Report of the Nyaga Committee, 1973; Bahl and Mant (1976); Report of the Civil Service Review Committee, 1979-80; Report and Recommendations of the Working Party on Government Expenditures, 1982; and, Sessional Paper No. 1 of 1986: Economic Management for Renewed Growth.

developing countries, Kenya does have a history of semi-autonomous local government. By and large, there is a viable institutional and legal structure in place, which could, with some reforms to be discussed later, permit local government to have an important role to play in the development process. Second, there has long been widespread official recognition by the Kenyan government that local authorities should be strengthened in order that they could fulfill their unique and important responsibilities more effectively. Finally, the unfortunate reality is that, in spite of the first and second points made above, there has been strong political resistance by the central government to any meaningful strengthening of local authorities. It is this obstacle that must be overcome if effective reform of local government will ever be able to occur in Kenya.

The Current System of Local Government in Kenya

Having reviewed the history and development of local government in Kenya, it is now appropriate to turn to a description of how the system operates. This includes a discussion of types of local authorities and their role in the overall public sector, as well as an explanation of how local authorities raise and spend resources and a description of the local authority debt situation.

Types of Local Authorities in Kenya

In 1977, the National Assembly passed The Local Government Act, Chapter 265 of the Laws of Kenya. This streamlined the organization of local authorities, laid out the functions, powers and responsibilities of different types of local authorities, and firmly established strict control of local authorities by the Minister for Local Government.

There are four types of local authority allowed in Kenya under the Local Government Act and its amendments of 1978, 1979, 1982, 1984, and 1988. Municipal councils are established in large urbanized areas and have substantial service provision responsibility. They provide many basic urban services, including roads, sanitation, water, sewerage, housing, and social services. As noted earlier, the largest of these councils are also required to provide primary education and health care. Town Councils are generally in smaller urban areas and do not have as much service responsibility. None are responsible for health and education, and few have water or sewerage schemes. Both municipal and town councils tend to provide some local revenue-generating services, such as markets, busparks, and slaughterhouses.

County Councils are in almost every case geographically identical with districts, the administrative subdivisions of the central government. The service area of a county council is all of the land area of its district not under the jurisdiction of a municipal or town council. County councils have had substantially fewer service responsibilities since being relieved of health, education, and road maintenance in 1970. They do provide social services, maintain some secondary roads, construct and operate market and slaughter facilities, and generally share in the provision of veterinary services.

The final type of local authority in Kenya is the urban council. These are in emerging urban centers being prepared for transition to town, and ultimately municipal, councils. They often provide marketing and other basic facilities but do not have full fiscal independence. They are under the jurisdiction of the county council in which they are located.

The local government revenue sources in Kenya are extremely diverse and vary greatly both across and within different local authority types. There is much less standardization of revenue sources than there is of service responsibilities for a particular type of council, and their assignment is much more arbitrary. A more detailed discussion of local authority revenue sources is presented in a later section of this chapter.

Local authorities in Kenya are governed by elected councils and managed by appointed administrative officers. They are highly regulated and controlled by the central government. There is little that a local authority can do without the approval of the Ministry of Local Government;

furthermore, the chief managing officers of the councils are actually central government civil servants under the Public Service Commission.

It is worth noting that a system of decentralized central government administration exists alongside the local government system. The country is divided into seven provinces under the leadership of provincial commissioners, and the provinces are divided into districts administered by district commissioners. The districts are divided further into divisions, subdivisions and locations, which are respectively run by district officers, chiefs, and sub-chiefs. The entire system, a holdover from the colonial administration, is under the Office of the President.

The central government's decentralized administration, usually referred to as the provincial administration, has often been in conflict with local authorities, because there is some degree of redundancy and ambiguity in their responsibilities, particularly at the district level. In 1983, President Daniel arap Moi introduced the District Focus for Rural Development strategy, which is supposed to strengthen the role of district administration in the development process. It is also supposed to coordinate the activities of district-level offices of central government agencies and local authorities through advisory boards known as District Development Committees. This new strategy has raised a number of important issues that will be addressed later.

The Structure of the Public Sector in Kenya

The central government is responsible for the vast majority of public spending in Kenya. It is heavily dependent on indirect taxes, such as sales taxes, export duties, excises, and import duties, which accounted for 59.4 percent of total recurrent revenue in fiscal year 1985/86. Income taxes raised another 30.2 percent of revenue in the same year. On the expenditure side, the four main categories are education, interest on public debt, general administration, and defense, which respectively accounted for 23.4, 19.8, 12.9, and 8.5 percent of total central government recurrent expenditures in fiscal year 1985/86.[6]

The relative importance of the central government in public spending has increased dramatically since the early days of independence. During the 1960s, local governments accounted for almost one-fifth of all public-sector spending in Kenya. After the transfer of certain local authority revenues and service functions to the central government in 1970, which was described earlier, the importance of most local authorities declined suddenly and dramatically. For example, aggregate county council expenditures fell by 85

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[6] These figures are calculated from data in: Economic Survey, 1987 (Nairobi: Central Bureau of Statistics, Ministry of Planning and National Development, Republic of Kenya, 1987), Chapter 6.

percent from 1969 to 1970 [Oyugi (1983), p. 134]. Local authorities in Kenya have never regained their former importance.

Table 4.1 provides information on Kenyan public revenues and expenditures in fiscal year 1985/86.[7] In that year, local government accounted for only 5.5 percent of total public-sector recurrent revenues and 5.0 percent of total government recurrent expenditures, with about 80 percent of this being provided by the 20 municipal councils. If only expenditures on goods and services are considered, local authorities accounted for 8.5 percent of the total, the bulk of which was again provided by municipal councils. The role of local government in capital expenditures was more significant. Local authorities accounted for 15.9 percent of total public sector gross fixed capital formation in 1985, with municipal councils alone accounting for 11.9 percent; however, it is important to note that the bulk of local authority capital financing comes from the central government's Local Government Loans Authority.

Thus, the local government sector does not have a very important fiscal role in Kenya relative to the central government. Nevertheless, municipal councils provide most of the major public services within their jurisdictions, and

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[7] In early 1988, the exchange rate between the Kenyan shilling and the U.S. dollar was approximately 17:1. One Kenyan pound equals 20 shillings, or about $1.18. The shilling is the basic unit of currency. Pounds are used only in official financial reports and documents.

TABLE 4.1

KENYAN PUBLIC REVENUES AND EXPENDITURES, 1985/86
BY LEVEL OF GOVERNMENT (MILLIONS OF KENYAN POUNDS)

LEVEL OF GOVERNMENT	RECURRENT REVENUES	RECURRENT EXPENDITURES	ADJUSTED RECURRENT EXPENDITURES*	CAPITAL EXPENDITURES**
Central	1186.36	1244.26	687.49	150.04
Municipal Councils	56.74	52.67	51.69	21.29
Other Local Authorities***	12.69	12.76	11.83	7.13
All Local Authorities	69.43	65.43	63.52	28.42
TOTAL	1255.79	1309.69	751.01	178.46
	PERCENTAGE DISTRIBUTION			
Central	94.4	95.0	91.5	84.1
Municipal Councils	4.5	4.0	6.9	11.9
Other Local Authorities	1.0	1.0	1.6	4.0
All Local Authorities	5.5	5.0	8.5	15.9

* Adjusted recurrent expenditures represent outlays for goods and services only (exclusive of transfers).

**Capital expenditures include gross fixed capital formation only. They specifically exclude loan repayments and transfers to funds.

***Town, urban, and county councils.

SOURCE: Economic Survey, 1987 (Nairobi: Central Bureau of Statistics, Ministry of Planning and National Development, Republic of Kenya, 1987), Chapter 6.

other types of local authorities provide services that are extremely significant to their constituents. Thus, the issue of the effectiveness of local authorities is of considerable importance to many Kenyans.

Description of the Local Authority Fiscal System in Kenya

This section provides a brief description of the Kenyan local government fiscal system in 1984 as a prelude to analyzing the fiscal role and operations of the local authorities. The composition and levels of revenues and expenditures across different types of local authorities are examined. This is followed by a look at the overall financial position of the various types of local government councils.[8]

Composition and Level of Revenues

Several Acts of Parliament, including the Local Government Act, the Rating Act, the Valuation for Rating Act and the Regional Assembly Act, give local authorities in Kenya the right to raise income from a wide variety of

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[8] The data used in this section come from field visits to a sample of Kenyan local authorities in 1986-87. A description of this fieldwork is presented in Chapter 5. Detailed information on site visits, definitions of revenue and expenditure categories, and problems with the data collection and analysis is presented in Appendices I, II, and III.

sources.[9] No particular sources of revenue are reserved exclusively for specific types of local authorities, but wide variations in the use of many sources of revenue across local authorities do exist for a number of important reasons. The composition of land in a local authority determines the extent to which rural and urban land taxes can be collected; furthermore, some types of services for which fees are charged are appropriate for some local authorities but not for others. Public veterinary services, for example, are often needed in rural areas, but only infrequently in urban areas. Conversely, sewerage systems are the norm in municipal councils, but are rarely operated in rural councils.

Another important reason for the variation in reliance on revenue sources across local authorities is that there are a variety of problems in revenue collection that make it very difficult to collect certain types of revenue in some local authorities. These will be discussed in detail in later chapters. In addition, there are wide variations in the economic base from which local taxes are derived. Some districts are highly productive agricultural areas abounding

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[9] The Regional Assembly Act of 1964 gave the regional assemblies formed under the Majimbo Constitution the right to levy a poll rate, which is a fixed fee head tax on all adult citizens living in the taxing jurisdiction. When the regional assemblies were dissolved, the poll rate was transferred to the local authorities. It is not widely used today because it is difficult to collect and because President Moi recently criticized some of the extreme tactics used by some local authorities to collect the tax.

with potentially rich sources of revenue. Others are arid or semi-arid with few or no very productive sources of revenue. Finally, the problem of different revenue capacities is sometimes a result of administrative decisions by the Ministry of Local Government or long delays in approving local authority by-laws, both issues to be dealt with in more detail later.[10]

Type of council and geographic location are the major factors that determine the principal revenue sources of a local authority.[11] As can be seen from the data in Table 4.2, municipal councils get most of their revenue from water charges, land rates, market fees, house rents, plot rents, slaughter fees and buspark fees. Large municipal councils are less diversified in their principal sources of revenue,

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[10] By-laws are documents registered with the Attorney General that give Local Authorities the legal power to raise revenue from the sources allowed to them in the Local Government Act and other legislation. Without a by-law for a particular source of revenue, the local authority has no legal authority to collect it.

[11] The categories of local authorities used in Tables 4.2 to 4.8 require some explanation. Data for all county councils is provided under the heading "County 1". "County 2" removes the counties which get more than 50 percent of their revenue from tourism. This has been done because the inclusion of these high tourism councils may distort some results. "Municipal 1" includes all municipal and town councils. "Municipal 2" excludes the largest municipal councils because they have responsibility for health care and primary education, so the composition of their revenues and expenditures would be expected to be significantly different from other urban local authorities. "Large Municipal" reports separate data for the large municipal councils, and "Town" reports separate data for the town councils, which tend to have fewer service responsibilities than most municipal councils.

TABLE 4.2

COMPOSITION OF LOCAL AUTHORITY REVENUES (1984)

Income Sources as a Mean Percentage of Total Income

by Type of Local Authority*

(Number in Parentheses Indicates the Number of Observations)

Income Source	County 1	County 2	Municipal 1	Municipal 2	Large Municipal	Town
Licences	12.0 (13)	13.5 (11)	13.8 (13)	16.4 (10)	5.0 (3)	20.1 (3)
Land Rates	18.9 (8)	24.6 (6)	21.3 (13)	21.5 (10)	20.6 (3)	16.3 (3)
Plot Rents	4.7 (11)	5.2 (9)	5.3 (8)	6.0 (7)	**	9.8 (3)
Cess	33.8 (11)	38.7 (9)	2.7 (7)	2.7 (7)	0.0 (0)	3.4 (3)
House Rents	2.5 (10)	2.7 (8)	10.3 (11)	8.2 (8)	16.1 (3)	6.6 (2)
Water Charges	0.4 (7)	0.3 (6)	24.5 (8)	26.0 (5)	22.0 (3)	0.0 (0)
Sewerage Fees	0.9 (2)	**	6.2 (10)	4.4 (7)	10.5 (3)	**
Market Fees	7.7 (13)	8.6 (11)	9.5 (13)	11.5 (10)	2.7 (3)	16.4 (3)
Slaughter Fees	1.7 (9)	1.8 (7)	4.7 (12)	6.0 (9)	0.8 (3)	4.0 (2)
Buspark Fees	0.1 (3)	0.1 (3)	5.7 (13)	6.9 (10)	1.6 (3)	12.1 (3)
Veterinary Fees	2.8 (11)	3.1 (9)	0.2 (3)	0.2 (3)	0.0 (0)	0.2 (2)
Works Fees	3.8 (9)	4.2 (8)	4.5 (13)	4.7 (10)	3.8 (3)	2.8 (3)
Poll Rate	3.2 (10)	3.9 (8)	1.9 (5)	1.9 (5)	0.0 (0)	2.6 (2)
Tourism Fees	25.9 (5)	4.8 (3)	0.0 (0)	0.0 (0)	0.0 (0)	0.0 (0)
Interest	6.9 (8)	8.8 (6)	4.0 (8)	3.4 (6)	5.7 (2)	**
Grants	8.9 (6)	12.0 (4)	21.0 (4)	**	23.6 (3)	**

* Definitions of Categories

County 1	= all county councils
County 2	= county councils without significant tourism (less than 10% of revenue derived from tourism)
Municipal 1	= all municipal and town councils
Municipal 2	= all municipal and town councils except large municipal councils responsible for health and and primary education
Large Municipal	= municipal councils responsible for health and education
Town	= town councils only

** means are not reported because there is only one observation

and tend to rely heavily on water charges, land rates, house rents, sewerage fees and grants for teachers salaries, with very small percentages of income coming from all other sources. Town councils rely less on land rates and infrastructure-based revenues than on plot rent and income from less capital-intensive services, such as market and buspark fees.

County councils tend to have fewer substantial sources of revenue than the local authorities in urban areas, except for those councils that are permitted to charge cess on cash crops or have significant access to land rates.[12] Most county councils rely heavily on market-related fees and trade licenses. Such fees are generally collected in divisional headquarters as well as the administrative seat of the county council. Some county councils have busparks and slaughterhouses, and a few collect large amounts of revenue from game reserves within their jurisdiction. A number of county councils also have access to house rents, poll rates, and a wide variety of other sources of revenue. Many of these, however, are often very unproductive or unreliable.

The geographic location of local authorities also has a significant impact on their revenue composition and capacity.

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[12] Cess is an ad valorem wholesale tax on agricultural production. It varies across crops and districts, but is normally in the range of one to three percent. The Government has recently announced its intention to standardize cess to a rate of one percent on a fixed set of crops in all districts.

Given the diverse agro-ecological conditions in Kenya, location is a prime determinant of economic base. Thus, it also determines the forms of economic activity that generate public revenues. The fertile areas in the central and western highlands are very productive, and agriculture-related taxes tend to generate significant amounts of revenue. Market fees and various types of cesses, where permitted, are excellent sources of funding in these areas. In much of the rest of Kenya, agricultural opportunities are more limited. Even though market fees may still be important for the local authority in these areas, they are much less productive than in more fertile regions. Semi-arid areas tend to be more dependent on livestock than on crops. Conditions permitting, livestock-related taxes, such as stock auction and slaughter fees, can be very important. In all of north-central and northeastern districts, miraa cess is one of if not the principal source of revenue.[13]

Per capita income from virtually all sources and in total is higher in municipal and town councils than in county councils, as can be seen from the data in Table 4.3. The largest municipal councils have much higher per capita income from land rates, house rent, interest, water charges,

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[13] Miraa is a green leafy plant that produces a mild stimulant effect when chewed. It is grown in certain parts of Kenya and is very popular, particularly among Moslems, because they are forbidden to take alcohol. Some local authorities in areas where miraa is popular have placed a levy, or cess, on the wholesale and retail sale of miraa, or on the export of miraa to other districts.

TABLE 4.3
MEAN PER CAPITA LOCAL AUTHORITY REVENUES (1984)
in Kenyan Shillings by Type of Local Authority*
(Number in Parentheses Indicates the Number of Observations)

	County 1	County 2	Municipal 1	Municipal 2	Large Municipal	Town
Income Source						
Licences	1.95 (13)	1.90 (11)	25.53 (13)	26.96 (10)	20.77 (3)	41.04 (3)
Land Rates	3.24 (8)	4.02 (6)	50.92 (13)	39.08 (10)	90.38 (3)	44.95 (3)
Plot Rents	.86 (11)	.67 (9)	10.40 (8)	11.56 (7)	2.32 (1)	21.40 (3)
Cess	8.02 (11)	8.06 (9)	3.36 (7)	3.36 (7)	0.00 (0)	5.03 (3)
House Rents	.61 (10)	.37 (8)	30.54 (11)	14.96 (8)	72.08 (3)	18.59 (2)
Water Charges	.10 (7)	.08 (6)	58.86 (8)	38.96 (5)	92.02 (3)	0.00 (0)
Sewerage Fees	.79 (2)	**	18.32 (10)	7.05 (7)	44.60 (3)	**
Market Fees	1.29 (13)	1.10 (11)	17.87 (13)	20.01 (10)	10.74 (3)	38.89 (3)
Slaughter Fees	.44 (9)	.35 (7)	7.75 (12)	9.23 (9)	3.30 (3)	12.97 (2)
Buspark Fees	.01 (3)	.01 (3)	8.96 (13)	9.76 (10)	6.30 (3)	16.95 (3)
Veterinary Fees	.44 (11)	.37 (9)	.20 (3)	.20 (3)	0.00 (0)	.24 (2)
Works Fees	.62 (9)	.63 (8)	9.15 (13)	6.90 (10)	16.65 (3)	3.72 (3)
Poll Rate	.39 (9)	.48 (7)	4.18 (5)	4.18 (5)	0.00 (0)	7.61 (2)
Tourism Fees	13.13 (5)	.56 (3)	0.00 (0)	0.00 (0)	0.00 (0)	0.00 (0)
Interest	2.38 (8)	3.05 (6)	11.83 (8)	8.06 (6)	23.17 (2)	16.35 (1)
Grants	1.57 (6)	2.36 (4)	77.92 (4)	**	101.09 (3)	**
Total	20.89 (13)	17.44 (11)	228.29 (13)	168.12 (10)	428.84 (3)	219.68 (3)

* Definitions of Categories

County 1 = all county councils
County 2 = county councils without significant tourism (less than 10% of revenue derived from tourism)
Municipal 1 = all municipal and town councils
Municipal 2 = all municipal and town councils except large municipal councils responsible for health and and primary education
Large Municipal = municipal councils responsible for health and education
Town = town councils only

** means are not reported because there is only one observation

sewerage charges, and works fees than do other municipal and town councils; however, these large councils have lower per capita income from licenses, plot rents, market fees, busparkfees, and slaughter charges.

Variation in per capita income and reliance on particular revenue sources are extremely great for virtually all sources of income for all different types of local authorities.[14] Some county councils, for example, get a majority of their revenue from land rates or agricultural cess, while others derive most of their income from trading license and market fees.

In summary, market fees, trade licenses and rents/rates tend to be important sources of revenue common to all local authorities. The relative intensity of their use depends largely on the composition of local economic activity. Use of these and other revenue sources also depends on the type of council, geographic location/agro-ecological conditions, and authority granted by the Ministry of Local Government. Tremendous variations in per capita income and the composition of income exist both across and within different types of local authorities.

Composition and Level of Expenditures

As might be expected, different types of local authorities in Kenya provide different types of services.

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[14] Details may be found in Smoke (June 1987).

This is true largely because of differing needs, input costs, human resources, and financial capacities. This section will present data on the variations in the composition and level of local expenditures within and across different types of local authorities.

The data in Table 4.4 indicate that county councils are fairly consistent in devoting most of their budget to expenditures on administration, social services, works, councillors expenses, markets, and veterinary services, although there is some diversity in the relative importance of each. A few county councils with game reserves also spend a significant portion of their budget on maintenance and operating expenses for these facilities.

Municipal and town councils spend the bulk of their resources on administration, works, water, housing, markets, and sewerage. Large municipal councils devote still higher percentages of their budgets to housing, and they must also spend heavily on primary education and health care, which they are required to provide. Town councils provide many of the same urban services as municipal councils, but few of them provide water and sewerage services.

The data in Table 4.5 demonstrate that mean per capita expenditures are higher in municipal and town councils than in county councils for all types of spending, without exception. The large municipal councils have substantially higher per capita spending than the smaller municipal and

TABLE 4.4

COMPOSITION OF LOCAL AUTHORITY EXPENDITURE (1984)

Expenditure Type as a Mean Percentage of Total Expenditure

by Type of Local Authority*

(Number in Parentheses Indicates the Number of Observations)

Expenditure Type	County 1	County 2	Municipal 1	Municipal 2	Large Municipal	Town
Administration	33.0 (13)	35.0 (11)	30.9 (13)	36.2 (10)	13.3 (3)	40.6 (3)
Engineer	**	**	5.1 (8)	6.1 (6)	2.2 (2)	0.0 (0)
Councillors	12.3 (13)	12.1 (11)	4.7 (13)	5.7 (10)	1.6 (3)	7.0 (3)
Primary Education	0.0 (0)	0.0 (0)	31.7 (3)	0.0 (0)	31.7 (3)	0.0 (0)
Social Services	17.2 (13)	18.9 (11)	6.3 (13)	6.9 (10)	4.3 (3)	5.6 (3)
Works	14.1 (13)	15.7 (11)	18.7 (13)	19.8 (10)	15.1 (3)	16.1 (3)
Housing	2.9 (4)	2.9 (4)	8.5 (11)	4.5 (8)	19.2 (3)	**
Water	1.4 (7)	1.1 (6)	14.4 (10)	13.8 (7)	15.7 (3)	**
Sewerage	0.9 (2)	**	5.4 (9)	5.4 (6)	5.4 (3)	**
Markets	9.9 (11)	10.7 (10)	7.9 (13)	9.2 (10)	3.6 (3)	17.1 (3)
Veterinary	4.6 (10)	4.3 (8)	2.0 (3)	2.0 (3)	0.0 (0)	1.8 (2)
Health	**	**	12.4 (3)	**	12.4 (3)	0.0 (0)
Slaughter	1.4 (5)	1.8 (3)	4.6 (12)	5.9 (9)	0.7 (3)	7.7 (2)
Tourism	14.1 (5)	2.7 (3)	0.0 (0)	0.0 (0)	0.0 (0)	0.0 (0)

* Definitions of Categories

County 1 = all county councils

County 2 = county councils without significant tourism (less than 10% of revenue derived from tourism)

Municipal 1 = all municipal and town councils

Municipal 2 = all municipal and town councils except large municipal councils responsible for health and and primary education

Large Municipal = municipal councils responsible for health and education

Town = town councils only

** means are not reported because there is only one observation

TABLE 4.5
MEAN PER CAPITA LOCAL AUTHORITY EXPENDITURE (1984)
in Kenyan Shillings by Type of Local Authority*
(Number in Parentheses Indicates the Number of Observations)

	County 1	County 2	Municipal 1	Municipal 2	Large Municipal	Town
Expenditure Type						
Administration	6.62 (13)	5.09 (11)	65.04 (13)	67.66 (10)	56.31 (3)	106.71 (3)
Engineer	**	**	9.00 (8)	9.08 (6)	8.79 (2)	0.00 (0)
Councillors	2.48 (13)	1.69 (11)	9.23 (13)	10.11 (10)	6.30 (3)	16.11 (3)
Primary Education	0.00 (0)	0.00 (0)	126.97 (3)	0.00 (0)	126.97 (3)	0.00 (0)
Social Services	3.34 (13)	3.02 (11)	11.79 (13)	9.98 (10)	17.83 (3)	10.13 (3)
Works	2.59 (13)	2.64 (11)	40.87 (13)	34.73 (10)	61.35 (3)	43.65 (3)
Housing	.40 (4)	.40 (4)	28.35 (11)	8.27 (8)	81.92 (3)	**
Water	.19 (7)	.12 (6)	35.23 (10)	21.18 (7)	68.02 (3)	**
Sewerage	.79 (2)	**	14.70 (9)	10.77 (6)	22.55 (3)	**
Markets	1.37 (11)	1.38 (10)	12.97 (13)	13.46 (10)	11.33 (3)	24.61 (3)
Veterinary	1.06 (10)	.62 (8)	3.08 (3)	3.08 (3)	0.00 (0)	1.48 (2)
Health	**	**	50.60 (3)	**	50.60 (3)	0.00 (0)
Slaughter	.44 (5)	.21 (3)	8.25 (12)	10.15 (9)	2.55 (3)	18.09 (2)
Tourism	10.11 (5)	.43 (3)	0.00 (0)	0.00 (0)	0.00 (0)	0.00 (0)
Total	18.41 (13)	15.02 (11)	224.46 (13)	172.86 (10)	396.46 (3)	232.91 (3)

* Definitions of Categories

County 1	= all county councils
County 2	= county councils without significant tourism (less than 10% of revenue derived from tourism)
Municipal 1	= all municipal and town councils
Municipal 2	= all municipal and town councils except large municipal councils responsible for health and and primary education
Large Municipal	= municipal councils responsible for health and education
Town	= town councils only

** means are not reported because there is only one observation

town councils in several major categories. This is particularly true for housing, works, water, and sewerage. It is also true for social services, despite the fact that larger municipal councils devote a smaller percentage of their total budget to these services than do smaller municipal councils. The large and small municipal councils have roughly comparable per capita spending for administration, engineering, and markets, while the larger councils spend substantially less per capita on slaughterhouses and councillors expenses.

The variations in expenditure composition within particular local authority groups are sometimes large, but substantially smaller than the variations exhibited by income composition, which were described above.[15] It thus appears that Kenyan local authorities of a particular type are somewhat consistent in the way they use their resources despite having very diverse revenue bases. There is, however, substantial variability in per capita expenditure figures within local authority groups.

The variations in per capita spending and expenditure composition within and across local authority types are partly due to differences in service needs. More urbanized and highly travelled local authorities might spend more on things like road surfacing and street lighting than other councils even if they are not very heavily populated. These

[15] Details may be found in Smoke (June 1987).

spending differences can also be partially explained by type of council and geographic location of the council. Municipal and town councils, for example, generally have greater responsibilities for providing public services than do county councils; furthermore, some councils need certain services more than others. A county council in livestock-intensive areas where certain diseases are a problem, for example, will spend more on veterinary services than other county councils. Some of these spending differences, however, depend heavily on variations in wealth and the types of revenues the local authority is permitted to raise. These issues, which are important in understanding local government finance in Kenya, will be discussed in greater detail in Chapter 5.

Financial Position of Local Authorities

This section examines the overall surplus/deficit position of Kenyan local authorities on their current accounts for fiscal year 1984.[16] It also explores how the surplus/deficit varies among different types of councils, how financial positions on the general fund differ from those on

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[16] Information on surpluses and deficits may often say very little about fiscal health. Some countries may not allow local authorities to incur deficits, and surpluses and deficits may only reflect accounting procedures. In the current case, these issues are not a concern or have been taken into account in the discussion. It is true, however, that surpluses and deficits say nothing about the ability of a government to provide the services required in its jurisdiction.

special-purpose funds[17], and the general debt position of local authorities.

Overall Surplus/Deficit

The overall financial positions on 1984 current accounts of the local authorities examined in this study are summarized in Table 4.6. There are two types of financial position considered: (1) general fund activities only; and, (2) all sources of income and expenditure. In the first case, Financial Position Type 1, activities for which there are separate funds are not figured into the calculations. Thus in the case of many municipal councils, income and expenditure on water, sewerage, housing and occasionally other services are excluded. For a few county councils, tourism revenues and expenditures are excluded. In Financial Position Type 2, all types of revenue and expenditure are included regardless of source.

In examining Financial Position Type 1 for 1984, it can be seen that eight county councils ran a surplus and five ran a deficit. It should be noted, however, that of the eight surpluses, two were in councils that normally run deficits,

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[17] As is the practice in many countries, urban local authorities in Kenya keep a general account (fund) and separate accounts (funds) for certain major services, including water, sewerage, housing, and, occasionally, other services. This is not only to keep separate records, but also to keep separate reserve funds for replacement investment in future years. Some county councils in Kenya also keep separate accounts for game reserves.

TABLE 4.6
OVERALL FINANCIAL POSITION OF LOCAL AUTHORITIES (1984)

A. Financial Position Type 1*

Type of Council	Number of Surpluses	Number of Deficits
County	8	5
Municipal	2	8
Large Municipal***	1	2
Town	2	1
Total	12	14

B. Financial Position Type 2**

Type of Council	Number of Surpluses	Number of Deficits
County	9	4
Municipal	5	5
Large Municipal***	3	0
Town	2	1
Total	16	12

* Financial Position Type 1 includes only general funds for municipal councils. Thus, municipal councils with separate funds for housing, water, sewerage, etc., will not have these revenues and expenditures figured into the surplus/deficit calculations. For county councils, game reserve income and expenditures would not be included here.

** Financial Position Type 2 includes all sources of revenues and expenditures for all types of councils.

*** Large municipal councils are also included in the category "municipal."

one was in a council that has run deficits since 1984, one was in a council that has run deficits in three of the past six years, and another was in a council that has budgeted for a deficit in fiscal year 1988. Thus, the number of surpluses seems to make the financial positions of the county councils studied look better than they are. In reality, only a handful of the county councils being considered run surpluses on a regular basis.

Among municipal councils, eight of ten ran a deficit on the general fund, while only two ran a surplus. Included in these ten are three large municipal councils with responsibility for health and education, two of which ran a deficit. Among the three town councils, two ran a surplus but one of these habitually runs a deficit and the one that ran a deficit in 1984 has been running surpluses since then. Overall, fourteen of the twenty-six local authorities in this study ran deficits on the general fund.

An examination of Financial Position Type 2 changes the situation somewhat. Only one additional county council runs a surplus when tourism revenue and expenditure are included in the analysis. However, when revenue-generating activities such as water and housing are included for municipal councils, three of the eight that ran deficits on their general funds now have overall surpluses. Because no town councils have separate funds, they are unaffected by considering Financial Position Type 2. Clearly, some councils are substantially helped by surplus revenue from separate funds, while others are not.

Surplus/Deficit Relative to Total Revenue and Population

The financial position of local authorities is further explored in Tables 4.7 and 4.8. Table 4.7 presents mean data on surplus/deficit as a percentage of total local authority revenue by type of local authority, while Table 4.8 gives mean per capita surplus/deficit by type of local authority.

Two types of surplus and deficit are reported in the tables: SD, which is the surplus or deficit for the general fund only. This excludes all separate funds and is the equivalent of Financial Position Type 1 in Table 6; and, 2) TSD, which is the surplus or deficit including all sources of income and expenditure. It is equivalent to Financial Position Type 2 in Table 4.6. Six statistics are presented in each table: number of observations, minimum, maximum, median, mean, and standard deviation.

The first thing that is apparent from these tables is the tremendous variation that exists in both the magnitude of surpluses and deficits as a percentage of total income and their per capita levels across and within all types of local authorities. Each of these figures will be examined in turn for all types of councils.

Surplus/Deficit as a Percentage of Total Revenue

As can be seen in Table 4.7, the financial positions of all county councils (County 1) show a mean deficit of -7.8 percent of total revenue, with the median being a surplus of 1.3 percent. The variation across councils is enormous, as is evident from the standard deviation of 42.2. When tourism finances are included in the analysis (TSD), the mean and median jump to respective surpluses of 3.3 and 8.3 percent.[18] Tourism clearly has an important impact on the financial position of at least some county councils.

The financial position on the general fund for all municipal and town councils (Municipal 1) reflects mean and median deficits of -7.3 and -11.0 percent, respectively. Again the variation is large as evidenced by the standard deviation of 18.3. When including revenues and expenditures from separate funds, such as water and housing, the mean and median improve significantly. Clearly there is a positive impact on some councils from including surpluses derived from separate fund activities.

Large municipal councils (Large Municipal) appear to do better financially than smaller municipal and town councils (Municipal 2). The small municipal and town council general

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[18] The mean and median surpluses are actually very slightly larger when excluding county councils with major tourism (County 2), but this is because one of the tourism councils has a large deficit on the general fund and continues to run a small deficit even after the game reserve surplus is included.

TABLE 4.7
SURPLUS/DEFICIT AS A PERCENTAGE OF TOTAL INCOME (1984)
BY TYPE OF LOCAL AUTHORITY

Type of Council*	Number	Minimum	Maximum	Median	Mean	Standard Deviation
County 1						
SD**	13	-125.5	36.6	1.3	-7.8	42.2
TSD***	13	-56.2	36.6	8.3	3.3	22.6
County 2						
SD	11	-56.2	36.6	1.3	2.6	25.1
TSD	11	-56.2	36.6	9.5	3.4	24.6
Municipal 1						
SD	13	-38.3	25.5	-11.0	-7.3	18.3
TSD	13	-38.3	25.5	0.7	-2.0	19.1
Municipal 2						
SD	10	-38.3	25.5	-17.5	-10.0	19.2
TSD	10	-38.3	25.5	-6.5	-5.8	19.3
Large Municipal						
SD	3	-11.0	15.9	-0.2	1.6	13.5
TSD	3	0.7	26.9	3.9	10.5	14.3
Town						
SD	3	-38.3	8.5	7.1	-7.6	26.6
TSD	3	-38.3	8.5	7.1	-7.6	26.6

* Definitions of Categories

County 1 = all county councils
County 2 = county councils without significant tourism (less than 10% of revenue derived from tourism)
Municipal 1 = all municipal and town councils
Municipal 2 = all municipal and town councils except large municipal councils responsible for health and and primary education
Large Municipal = municipal councils responsible for health and education
Town = town councils only

** SD is the surplus or deficit on the general fund. It excludes all separate fund revenues and expenditures, including water, sewerage, and housing for some municipal councils, councils, and game reserve income for county councils.

*** TSD is the total surplus or deficit resulting from the consideration of all sources of income and all types of expenditure.

funds (SD) show respective mean and median deficits of -10.0 percent and -17.5 percent, while the large municipal council mean and median are 1.6 and -0.2. Both groups show significant cross-council variation, but it is larger for the small municipal and town councils.

When considering all sources of revenue and expenditure (TSD), the mean and median deficits for small municipal and town councils decline, but remain significant (-5.8 and -6.5 percent). The financial position of large municipal councils improves, registering mean and median surpluses of 10.5 and 3.9 percent. Thus, the financial position of larger municipal councils improves more from separate fund surpluses than does the average small municipal council.[19]

Per Capita Surplus/Deficit

The data on per capita surplus/deficit by type of council are presented in Table 4.8. In a few cases, the sign and magnitude of the figures in this table differ from the figures on surplus/deficit as a percentage of total income presented in Table 7. For example, county councils show a mean deficit of -7.8 percent of income, but a mean per capita surplus of K.Sh. 0.78. There are not, however, many

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[19] It is true, of course, that only three large municipal councils of the eight in the country are considered and only one has a substantial surplus. It is also true, however, that none of the large municipal councils has a very large deficit, even on the general fund, while many smaller municipal councils do have substantial deficits, even when all sources of income and expenditure are considered.

TABLE 4.8
PER CAPITA SURPLUS/DEFICIT BY TYPE OF LOCAL AUTHORITY (1984)
(in Kenyan Shillings)

Type of Council*	Number	Minimum	Maximum	Median	Mean	Standard Deviation
County 1						
SD**	13	-10.56	18.06	0.29	0.78	6.58
TSD***	13	-3.40	18.06	1.18	1.98	5.39
County 2						
SD	11	-3.40	18.06	1.18	2.35	13.27
TSD	11	-3.40	18.06	1.39	2.43	5.67
Municipal 1						
SD	13	-73.62	50.02	-14.63	-9.37	36.84
TSD	13	-73.62	84.07	3.29	4.74	38.65
Municipal 2						
SD	10	-73.62	48.38	-16.35	-12.21	35.07
TSD	10	-73.62	48.38	0.90	-4.72	33.96
Large Municipal						
SD	3	-48.60	50.02	-1.13	9.40	49.32
TSD	3	3.29	84.70	20.77	36.25	42.85
Town						
SD	3	-73.62	28.45	5.45	-13.24	53.54
TSD	3	-73.62	28.45	5.45	-13.24	53.54

* Definitions of Categories

County 1 = all county councils
County 2 = county councils without significant tourism (less than 10% of revenue derived from tourism)
Municipal 1 = all municipal and town councils
Municipal 2 = all municipal and town councils except large municipal councils responsible for health and and primary education
Large Municipal = municipal councils responsible for health and education
Town = town councils only

** SD is the surplus or deficit on the general fund. It excludes all separate fund revenues and expenditures, including water, sewerage, and housing for some municipal councils, and game reserve income for county councils.

*** TSD is the total surplus or deficit resulting from the consideration of all sources of income and all types of expenditure.

striking major differences between the overall patterns exhibited by the two sets of data. For that reason, the per capita figures will not be discussed in any detail.

The principal conclusions reached from an examination of the per capita figures are basically identical to those derived from an examination of the surplus/deficit as a percentage of income figures. These are: (1) The inclusionof income and expenditure figures from separate fund accounts tends to improve the overall financial position of most local authorities for whom it is relevant, although some of the councils continue to run a deficit; and, (2) Large municipal councils on average do better with both their general and separate fund accounts than do smaller municipal councils, a majority of which continue to run a deficit even after separate fund accounts are considered. This may reflect a variety of factors, including greater efficiency in service provision or better revenue collection in larger municipal councils. It may also reflect less positive factors as well. Larger councils tend to have large reserve funds from water and housing accounts that have been built up over the years. Some of these councils seem to use internal transfers as income to offset expenses for some services that are not self-financing. Furthermore, one of the large municipal councils appears to get more revenue from grants for teachers salaries than it spends for primary education, indicating that the Ministry of Education is subsidizing other municipal services. These factors may make some large municipal councils appear to be in better financial shape than they actually are.

Now that the financial position of Kenyan local government has been briefly described, several important points need to be raised regarding local authority fiscal health. First, recent evidence indicates that the financial positions of some local authorities, including a number of the largest municipalities, have been steadily deteriorating in the last few years. Second, interviews with local authority officials and examination of local authority financial records indicate that deficits in local authorities are frequently financed by drawing down the reserve funds of such separate accounts as housing and water. In some cases, these reserve funds, which have been built up over the years, are being depleted at an alarming rate. This raises the question of how these councils will manage when their reserve funds are fully drawn down; furthermore, the purpose of these reserve funds is to set aside money for replacement investment, not to finance deficits on the general fund. Finally, the Ministry of Local Government is not supposed to approve budget estimates that reflect a deficit, so most councils write their estimates to reflect a surplus. An examination of budgeted versus actual figures for 1984 in about a dozen councils indicates that these two sets of figures often bear little resemblance to each other. Budget estimates often overstate revenues and sometimes understate expenditures. Some councils essentially construct a budget reflecting a surplus to gain Ministry approval, knowing full well that they are likely to run deficits, which must be financed by drawing down reserve funds or securing bank overdrafts.

Local Authority Debt

It is extremely difficult to get any reliable information on the indebtedness of local authorities in Kenya, primarily for two reasons. First, debt is a very sensitive issue with local authority officials. Some local authorities are deeply in debt and far in arrears on their repayments, and they are unwilling to discuss the issue, especially with someone who comes as a representative of the Ministry of Local Government. Second, the Local Government Loans Authority (LGLA), a parastatal agency within the Ministry of Local Government that provides the vast majority of capital financing for Kenyan local authorities, is extraordinarily disorganized and does not keep proper records or bill local authorities for their repayments.[20] The LGLA is directly controlled by the Minister for Local Government.

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[20] LGLA accounts are currently being updated by a private accounting firm and statements are being sent to all local authorities. The same firm is exploring options for reorganizing the LGLA into a well-managed and financially viable municipal development bank, which will be discussed later.

Despite the inability to get accurate data, it is clear that the local authority debt problem is of staggering proportions. Recent estimates indicate that local authorities owe the LGLA more than two billion Kenyan Shillings, at least several hundred thousand of which are in arrears. The local government debt issue is very complex because it is tied into a major intergovernmental problem, the failure of central government ministries and parastatals to pay rates and charges due to local authorities.[21] This will be discussed later in this thesis.

The Future of Local Authorities in Kenya

As has been demonstrated earlier in this chapter, Kenyan local authorities are a diverse group with significant financial problems, and there has long been some degree of controversy about an appropriate role for them. Certain factions in the current Government of Kenya would undoubtedly like to see the responsibilities of local authorities further reduced, with some going so far as to advocate the abolition of county councils. There is a possibility that this could happen, but it seems an unlikely move in the foreseeable future.

At the present time, there is also significant support in Kenya for reforming the local authorities. The discussion

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[21] Unlike in the United States, the central and local governments in Kenya are not exempt from each other's taxes.

in Chapter 1 about reasons for interest in strengthening local government in the developing countries is very much applicable to Kenya. In particular, the central government has been growing too rapidly and is trying to reduce its expansion at a time when the rate of population growth is the highest in the world and the demand for services is growing rapidly. Furthermore, large central government deficits and debt burdens require a more cautious attitude toward new and expanded central government responsibilities.[22] Local authorities are seen as an underutilized source of revenue and administration, so an expanded role for them seems attractive.

The Government of Kenya is also embarking on a new decentralized growth strategy that will substantially increase the responsibilities of many local authorities in areas where they have traditionally been weak. Sessional Paper No. 1 of 1986, "Economic Management for Renewed Growth", outlines a rural-urban balance development strategy designed to encourage widespread growth in Kenya by promoting linkages between rural agricultural areas and a hierarchy of urban centers. The document criticizes past urban and spatial development policy for focusing on location and settlement patterns in isolation rather than in the context of rural-urban linkages and overall macroeconomic conditions

[22] The 1986/87 deficit was originally planned to be 200 million Kenyan pounds. The actual figure was just over 400 million pounds, or 8 percent of gross domestic product.

and priorities.

The new rural-urban balance strategy intends to focus scarce Government of Kenya resources in designated small trading centers located in high potential, underurbanized rural areas known as Rural Trade and Production Centers (RTPCs). Resources will be used to provide basic packages of infrastructure as well as services and facilities designed to support the growth of agricultural and non-agricultural (primarily informal sector) activities in these centers and their surrounding hinterland. Thus, the policy is designed to strengthen both sectoral and rural-urban linkages and to stimulate multiplier effects. Up to 80 RTPCs are expected to be initiated during the next ten years.[23]

The RTPC Programme will be implemented at a decentralized level through the District Development Committees and will require a great deal of support from the districts and local authorities. Although design and construction of the RTPCs will be coordinated largely by district-level offices of the central government, local authorities are expected to play a key role in the planning process. More importantly, local authorities will have primary responsibility for ownership, maintenance and recurrent costs of most of the facilities constructed under the RTPC Programme.

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[23] More information on the Government of Kenya's rural-urban balance strategy is presented in Appendix IV.

In order for Kenyan local authorities to be able to meet their expanding development responsibilities in the coming years effectively, the Government of Kenya must direct serious effort towards increasing their viability. If this is to be accomplished, two major issues need to be confronted.

First, a consensus on the basic role and functions of local authorities in Kenya needs to be reached and explicitly articulated. This is something that has never been done despite decades of debate on the matter. Second, if local authorities are to be expected to fulfill their designated service responsibilities and perhaps assume new ones, a number of persistent problems need to be understood better and more effectively dealt with. These include ensuring access to sufficient sources of income, improving revenue collection, strengthening the managerial capacity of local authority officials, and correcting institutional and procedural problems in central government ministries and agencies which affect the performance of local authorities. Each of these issues will be discussed in subsequent chapters as part of an evaluation of the Kenyan system of local government.

Having outlined the history and described the current structure and possible future role of local government in Kenya, the next chapters will use the analytical framework outlined in Chapter 3 to define an appropriate fiscal role for Kenyan local authorities and to evaluate how well the current system in Kenya fits that role.

CHAPTER 5

ANALYSIS AND EVALUATION OF THE FISCAL ROLE OF LOCAL GOVERNMENT IN KENYA, PART I: PUBLIC FINANCE ISSUES

The framework outlined in Chapter 3 for analyzing and evaluating the fiscal role of local government in developing countries will be applied to Kenya in this and the following chapter. This chapter focuses on the major public finance issues: service provision, revenue generation, and revenue-expenditure linkages. Chapter 6 deals with issues related to institutional organization and capacity, which affect the ability of the system to meet public finance objectives. Before beginning the analysis, a brief description of the fieldwork on which the analysis is based is presented.

Fieldwork Sites and Methodology

The data and information analyzed in Chapters 5 and 6 were collected between July and December of 1976 in a series of field visits to a sample of Kenyan local authorities. The sample was selected by the Ministry of Local Government to be broadly representative of different types of local government and different regions/agro-ecological zones in Kenya. The focus was on municipal and county councils, but a few town councils were also visited. At the time of sample selection, there were 84 local authorities in Kenya, so that the sample of 26 covers almost one-third of the total number.[1]

Thirteen of 39 county councils (33 percent), 10 of 20 municipal councils (50 percent), and 3 of 7 town councils (43 percent) were visited. None of the 18 urban councils, which are fledgling local authorities technically under the jurisdiction of county councils, were included. The research covered local authorities in 7 of 8 provinces (excluding Nairobi Province) and in 19 of 41 districts (excluding Nairobi, Mombasa, and 20 other Districts). Appendix I contains additional details on the local authorities included in this study.

A typical visit to a local authority lasted at least several days. Copies of budget estimates were obtained from each council, and the treasurer normally provided access to other financial records. Financial, managerial, and institutional issues were discussed in-depth with appropriate local authority officials, and site visits were made to local authority facilities and projects, as well as to divisional headquarters in some of the county councils.

Because of numerous data collection and availability problems, the quantitative analysis in this research focuses on only one year of data. This is 1984, the most recent year

[1] Since the completion of the data collection, the Minister for Local Government has created 22 new urban councils and upgraded 12 former urban councils to town council status. The number of municipal and county councils, the principal units of local government, has remained unchanged. Thus, as of early 1988, there are 106 local authorities, but some of the new ones are not yet functioning.

for which actual, as opposed to budgeted, financial data are generally available.[2] The financial data categories used throughout the analysis are defined in Appendix II, and the major conceptual and empirical problems encountered with the data are explained in detail in Appendix III.

In addition to collecting information from local authorities, in-depth interviews were conducted with officials from the central office of the Ministry of Local Government, all of the provincial local government officers stationed in the provincial capitals, and officials of other ministries related to the functioning of local authorities. Data relevant to local authorities were collected from the Ministry of Local Government, the Ministry of Lands and Settlement, and the Ministry of Planning and National Development. These efforts, which were conducted between January and July of 1987, provided various types of data and information, including personal opinions and observations. This report uses all of these quantitative and qualitative sources of information in analyzing the situation and drawing conclusions about the fiscal role and operation of local

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[2] This is not an ideal year for the analysis because the country experienced a severe drought during it, but data for a more recent year were not available at the time the fieldwork was conducted. Use of an earlier year would have been complicated by the fact that, during the early 1980s, local authorities were in the process of converting from a calendar fiscal year to the central government's fiscal year (July 1 to June 30). Local authorities made this change at different times, so that it was not possible to find an earlier year when all local authorities in the sample were using the same fiscal year without going back to the 1970s.

authorities in Kenya.

Evaluation of Public Finance Objectives

The framework, defined in Chapter 3, outlined three public finance areas that need to be examined in evaluating the fiscal role of local government. These are: service provision, revenue generation, and revenue-expenditure linkages. Each of these will be examined for Kenya using the guidelines developed in Chapter 3.

Expenditures and Service Provision Issues

The basic function of a local authority is to provide services to the people living in its jurisdiction. The logic behind the assignment of service responsibility to local authorities in Kenya will be discussed in this section. In addition, there will be an examination of some of the major issues related to local service provision, the most important of which is the factors affecting the variations in the level of expenditure made by the different types of councils.

Assigning Services to Local Authorities

Data presented in the previous chapter demonstrated some variations in the composition of local authority expenditures on services and suggested some possible explanations for them. To what degree are these variations based on the assignment of certain services to local authorities? In fact, the Government of Kenya actually assigns very few mandatory services to local authorities.[3] Seven of the largest and oldest municipal councils[4] are required to provide certain services, including health care, education, and roads within their jurisdiction, but only a few minor caretaking services, such as providing for the burial of destitute persons who die in their jurisdiction, are required by law of all local authorities. Most local authority functions set forth in the Local Government Act are permissive, i.e., the local authorities may undertake the provision of these services if they wish, sometimes with the stipulation that such provision must be according to the specifics of another law or with the consent of an overseeing ministry. For example, any local authority in Kenya may be a water undertaker if the Ministry of Water Development gives formal consent. The Minister for Local Government may make permissive functions mandatory by administrative directive, but this power in not exercised frequently.

Given this situation, the assignment of functions to local authorities in Kenya is often by custom or historical accident, or is decided simply on the basis of what the

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[3] More information on the mandatory versus the permissive functions of local authorities in Kenya may be found in: Oyugi (1983), and Akivaga, Kulundu-Bitonye, and Opi (1984).

[4] The seven municipal councils with responsibility for health and education are: Nairobi, Mombasa, Kisumu, Nakuru, Eldoret, Thika, and Kitale.

council can afford and needs, and whether particular services are being provided by the central government or the private sector. There were attempts in the 1960s and 1970s to define and standardize the types of services that should be provided by rural councils and urban councils of different types and sizes, but little effort was made to enforce these guidelines or assist the local authorities in complying with them.[5] Because of this, there is some degree of diversity in the major types of services undertaken by local authorities, particularly by the rural and smaller urban councils.

Although little formal service assignment to local authorities actually takes place in Kenya, the criteria developed in Chapter 3 can be used to make some observations about the pattern of local government service delivery that has evolved since the colonial era. It is first important to note that in the Kenyan context, very few services are truly local in the sense that varying preferences exist which dictate the need for providing them at a decentralized level. Because of the geographic dispersion of local authorities and the largely local impact of some services, however, it is possible to make a convincing argument for providing them at the local level. Examples of these types of services include

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[5] The most recent definition of the different types of settlements and the types of services they are supposed to provide is found in: Government of Kenya, Human Settlements in Kenya: A Strategy for Urban and Rural Development (Nairobi: Ministry of Lands and Settlement, Republic of Kenya, 1978).

trash collection, sewerage/pit latrines, street lighting, fire services, social services[6], and local roads. In addition, a strong case can be made for local authorities, particularly in the rural areas, to provide some private-sector-type facilities and services that are not provided by the private sector. Such activities include market places, slaughterhouses, housing[7], and livestock auction yards. In fact, most local authorities in Kenya do provide many of these services.

At the other end of the spectrum are some services for which there are clear economies of scale or interjurisdictional externalities, and for that reason they should be provided centrally. Such services are, in fact, provided centrally in Kenya by parastatals or central

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[6] "Social services" in Kenya is normally used to classify a wide variety of miscellaneous community services, including pre-primary education, community centers, local public sports facilities, orphanages, and parks. Most of these services are very local in nature. Although for some of them, such as orphanages, it may be justifiable for the central government to intervene on equity grounds, self-help fundraising is more likely to be a more workable solution to funding problems, particularly in the rural areas.

[7] In some developed countries, housing is seen as a basic need and is therefore provided at subsidized rates for those who cannot afford other options. Housing is rarely provided as a public service in that sense in Kenya, except in a few of the largest cities. Housing needs are very simple in most areas, and there is a great deal of sharing among extended family and friends. Public housing in Kenya is normally provided for one of two reasons: (1) as a service for civil servants or local authority employees; or (2) as a revenue-raising enterprise for the local authorities, who have found that they can normally earn a healthy surplus by providing housing in urban centers, often for middle- and higher-income residents of their jurisdiction.

government ministries. Examples include electricity and telephone service, which are provided in Kenya by two national parastatals, Kenya Power and Lighting Corporation and Kenya Posts and Telecommunications Corporation. Other more obviously public services are also provided centrally, such as primary national trunk roads, which are the responsibility of the Ministry of Transport and Communication. This Ministry also coordinates the system of all types of roads for the entire country.

In between the obvious local services and the obvious national services are a whole range of services which have both local and national qualities. In such cases, the assignment of responsibility is much less clear, and it is probably decided largely on the basis of political judgments, which are sometimes defensible and sometimes questionable. Examples of such services are: health, education, social services, water, and veterinary services.

Health and education, two of the major public services in Kenya, are both goods that can be considered local to some extent, because it is clearly possible for preferences and needs for them to vary widely across jurisdictions. However, in most countries around the world there is some central government involvement in the provision of these services, both because they generate positive externalities and serve national goals, and because there are equity considerations in providing an invariant minimum level of these services.

Kenya, like most developing countries, is still striving to provide minimum levels of education and health care to its people, so a strong case can be made for the central government to intervene at least to the extent of providing standards and financial assistance. In Kenya, however, the central government completely controls the provision of health and education services except in the eight largest municipalities.

It is very difficult to justify the extreme degree of central control over education.[8] There are qualified teachers all over Kenya, and it would be possible to establish minimum standards for all schools and still allow different local areas to tailor the curriculum to local needs. The probable main reason why this is not done is that the central government wishes to maintain strict control over the educational system. This was clearly articulated by the Luo leader, KANU Secretary General and Minister for Justice and Constitutional Affairs Tom Mboya in a speech to the

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[8] If local preferences for education vary widely and mobility is high, the efficiency loss from central provision of education may be significant. There is no good information available on educational preferences in Kenya. It seems likely, however, that some heterogeneity of preferences should be expected. Although preferences for training in basic skills are probably fairly homogeneous (and, in any case, there is an externality issue here), there are significant cultural and language differences in different parts of the country. Furthermore, the types of skills that need to be taught in vocational schools and polytechnics will vary to some extent with differences in economic base and other local conditions. Thus, a case can be made for some local control over education.

National Assembly in the late 1960s, shortly before the central government took responsibility for education away from the local authorities. He stated:

> There is a need to have more government say and control in the education of the people of the country. We can no longer continue with the system by which you have pockets of authority all over the country, deciding what and how to conduct education throughout the country. There must be established a definite area of government control if we are going to implement our policies.[9]

It is not as easy to make a case for some local control over health care, except perhaps for simple dispensaries that provide treatment for minor illnesses and injuries. The health care system is not as advanced as the educational system in Kenya, and there are many areas where basic needs are not being met. There is a national shortage of qualified medical personnel and most local private sector providers in many areas only practice traditional medicine, so that it would be difficult to find people to staff health centers and dispensaries in some areas if they were not posted there by the central government. Thus, the government's centralization of the health care system in Kenya is relatively easy to justify.

Some of the other major public services in Kenya have both local and national characteristics. Services such as water and veterinary health care can be provided locally and often are in Kenya, but there is also some justifiable

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[9] National Assembly, Official Record, January 8, 1968, column 3522.

central government involvement. Water is a basic human need, which is often difficult to obtain in many parts of Kenya, particularly at certain times of year. If local authorities have the capacity to provide water reliably, there is no need for the central government to get involved unless there are externalities or scale economies involved. If local government does not have the required capacity, a strong case can be made for intervention by the central government. Water in Kenya is provided by local authorities in some areas and by the Ministry of Water Development (MWD) in others. There are, however, no clear guidelines for deciding whether a local authority or the Ministry will be the water provider in a particular area--this decision is left entirely to the discretion of the Minister for Water Development. This has led to a situation in which some local authorities who are probably capable of providing water have been refused permission to do so by the MWD. Other local councils who have the authority from MWD to provide water cannot provide the service adequately. This is a contentious issue not only because of the service implications, but also because water is often a good source of surplus revenue for local authorities.

Another reason why water is so important is the fact that it must be provided jointly with some other services in order for those services to operate effectively. Health centers, schools, slaughterhouses, sewerage systems, cattle dips, and other services require water on a regular basis. There are cases in which these facilities have been built without first planning to insure that an adequate supply of water would be available. In some cases, water must be provided by the same level of government as certain other services, or coordination and service provision problems will arise. For example, some municipalities are sewerage providers, but not water providers. Without control over the water supply, these local authorities cannot force people to pay their sewerage charges unless the Ministry of Water Development cooperates.

A somewhat ambiguous assignment situation exists with the provision of veterinary care in Kenya. Some types of veterinary health services, particularly facilities such as crushes and dips[10], can be provided by local authorities in rural areas, and in many cases are. When local authorities cannot afford to provide such facilities in areas where they are needed, a strong case can be made for central government financing or provision because of the potential externalities and costs to the local economy involved in livestock diseases. However, although there are guidelines, the Ministry of Livestock Development (MLD) seems to be fairly

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[10] Crushes are small structures used to restrain livestock when vaccinating them or treating them for a disease. Dips are long narrow pools filled with water and chemical solutions that repel ticks and other parasitic insects that spread diseases. During certain seasons of the year when insects are prevalent, livestock must be forced to swim through the dip once every week or so.

arbitrary in what it requires of local authorities and what it provides centrally. In some cases, for example, local authorities must construct, staff, and operate cattle dips. In other cases, the Ministry constructs the dips, but requires the local authorities to operate them. In still other cases, the MLD constructs, staffs, and operates the dips. There is sometimes little correlation between need for dips, the local authority's ability to finance the dips, and the degree of MLD involvement. In some cases, the Ministry provides the whole package in relatively wealthy areas and provides little or no assistance in poor areas with a need for the services.

Turning from specific services to specific types of local authority, the observed pattern of service provision across different types of local councils is generally reasonable. As has been shown earlier, councils in urban areas provide many traditional urban public services, such as sewerage, water, trash collection, street lighting, etc. Some of the largest and oldest municipal councils have been assigned greater responsibility than their smaller and newer counterparts in the areas of health and education. In the rural areas, local authorities tend to provide services related to basic human requirements as well as agricultural and livestock needs. Local authorities in both urban and rural areas provide certain entrepreneurial services that serve the dual need of filling in where the private sector fails and raising, at least in some cases, a substantial volume of revenue.

Thus, although it is possible to make a case on economic grounds for assigning additional service responsibilities to some local authorities, particularly county councils, the service role of local authorities that has developed in Kenya over the years, with a few prominent exceptions, makes a lot of sense. There are, however, numerous difficulties with the actual operation of many services. Most of the problems that have arisen in local service provision have been not as a result of improper assignment or self-assignment of public services to local authorities, but due to a lack of local authority capacity to provide the services that should logically be their responsibility. The primary problems have been inadequate revenue, poor management, and lack of skilled personnel to provide the services. These issues will be discussed in this and the next chapter, while possible improvements in local authority service assignment will be discussed in Chapter 7.

Variations in Per Capita Total Expenditure

Having dealt with the composition of local authority expenditures, it is appropriate to turn to the issue of expenditure levels. It is clear from the information in the previous chapter that there is significant variability in the level of expenditures within and across different types of councils. The general differences across the various types of council can be largely explained on the basis of different service responsibilities. This section uses regression analysis to try to identify the factors that seem to be most highly related to variations in per capita total expenditure on services within council groups in order to see if there is some reasonable and/or discernable basis for them. Various demographic and economic characteristics of local authorities were explored in order to measure their degree of association with per capita total spending. Among those frequently used by local finance analysts to explore local spending patterns are size (population), per capita wealth, and population density (population per square kilometer). These variables were selected because they are expected to have an influence on the demand for local authority services, and/or costs of service provision, and/or the ability of local authorities to raise revenue.

It should be noted that the simple reduced-form model used in this analysis, a basic version of which was first estimated for the United States in the 1960s, has been much improved upon by more recent analysts. The simple model does not separate the demand and supply sides, and it is plagued by various econometric problems.[11] The reduced-form

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[11] The simple methodology on which this is based was first used by Fisher (1961) in an attempt to explain variations in state and local government per capita

model is used here because the data necessary to estimate a more adequately specified model are not available for Kenya. Even the simple specification, however, sheds some light on the determinants of local government spending.

Higher population might be expected to exert a positive influence on spending for several reasons. The demand for local services may rise as population increases because of a wider variety of preferences. In part, higher spending for public services in populous local authorities may be a reflection of higher costs, which are due to congestion. In addition, the number of public services provided is likely to be greater in high population areas. There are certain fixed costs involved in the provision of any service, and it may not be efficient to provide some services until population reaches a certain size. Thus, more populous jurisdictions have a wider range of services and higher levels of spending, a phenomenon dubbed the "zoo effect" by Oates (1986, p. 9). Finally, the degree of bureaucratic power, which can affect spending mix and levels, may be positively associated with population size.

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expenditures in the United States. This research was followed by a variety of other investigations on the same topic, which have come to be collectively known as the "determinant" studies in state and local finance. There are a variety of significant problems in the specification of the equation (Bahl, 1968), but it is adequate for the present purpose of getting a rough idea of association between spending levels and other variables in local authorities. More recent models of supply and demand for local government services are summarized and critiqued in Oates (1986).

Wealth (property valuation) is expected to be of importance because wealthier councils are likely to have the ability and desire to raise more money than poorer councils to provide services. High property values are often associated with more densely and highly developed land, which occurs in areas where there is a high level of economic activity. This activity generates a high demand for services, as well as high levels of local authority revenue from property taxes, business-related taxes, marketing fees, and charges for public services, such as water, sewerage, and trash collection.[12]

The impact of population density on local public spending is not always clear. Densely populated areas might have reduced costs because of potential economies of scale in providing services on a larger scale to a more densely clustered target population. Alternatively, density could raise the costs of some types of services because of congestion.

The local authority expenditure regressions in this analysis were, for the most part, run separately for county

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[12] Income may affect the supply side of service provision because of its observed inverse relationship with costs in certain cases. This suggests that higher income may have a negative effect on per capita spending for some services. Because income and wealth would be expected to be highly correlated, the same may be true for wealth, although the various positive effects of wealth on spending levels may overshadow this effect in the aggregate. A detailed discussion of the effect of income on the supply side of local public services is provided in Oates (1986).

and municipal councils. This was done for a variety of reasons, the primary one being that municipal and county councils are very different entities with different principal sources of revenue and different service responsibilities. Different factors might be expected to influence spending in the two cases. Furthermore, wealth is defined differently for municipal and county councils, and some of the data used in this analysis were available for only one or the other type. The problem with doing the regressions separately for county and municipal councils is that the number of observations in each group is small. Nevertheless, the analysis yields some unambiguous results from which certain generalizations can be made.

County Councils[13]

It might be expected that certain basic county characteristics would influence the level of spending by county councils. The initial analysis used as explanatory variables the local characteristics discussed above. In

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[13] There is much more economic and demographic data available for county councils than for municipal councils. This is because county councils are, for the most part, geographically identical to districts, the administrative subdivisions of the central government. Various data have been collected at the district level for years, and they have become more readily available because of the growing interest in district-level research precipitated by the District Focus for Rural Development strategy initiated in 1984. This strategy is an attempt to deconcentrate planning and implementation responsibility for development projects to the district level. It was introduced in Chapter 4 and will be discussed in greater detail in the next chapter.

fact, population, per capita wealth, and density have very little association with the level of per capita spending in county councils, either separately or together. The regression results in Table 5.1 show that all of the variables are highly insignificant, and the overall power of these variables to explain the variations in per capita spending across councils is effectively nil, as evidenced by the coefficient of determination (R-squared) of -.188.[14]

These results, in fact, are not at all surprising in the Kenya case. The population figures used in this analysis, as explained in more detail in Appendix III, are not good measures of serviced population, particularly in county councils. The percentage of total population benefitting from county council services no doubt varies dramatically across councils and types of service, and there is no practical way to get accurate, disaggregate serviced population figures.

The low significance of wealth results from a variety of factors. As explained in greater detail in Appendix III, the measure of wealth used in this analysis is not entirely satisfactory. It measures the per capita surplus of county councils by aggregating sales of livestock and agricultural

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14 The high degree of multicollinearity among the explanatory variables undermines the significance of any one variable. This is not, however, an important consideration here because multicollinearity does not affect the overall explanatory power of the regression, which in this case is so low that it is clear that the relationships are insignificant both individually and collectively.

TABLE 5.1
REGRESSION 1 FOR PER CAPITA TOTAL EXPENDITURES IN COUNTY COUNCILS

Explanatory Variable	Coefficient	T-Statistic	Standard Error
Population	-0.000014393	-0.610	0.000023611
Per Capita Wealth	-0.00017976	-0.043	0.004165500
Density	0.008924600	0.169	0.025658000

Intercept	: 23.87797
Coefficient of Determination (R-Square)	: 0.109
Adjusted R-Square	:-0.188
Multiple R	: 0.330
Standard Error of Estimate	: 14.727

Correlation Coefficients for Explanatory Variables

Population and Per Capita Wealth	: 0.614
Population and Density	: 0.851
Per Capita Wealth and Density	: 0.502

produce to state marketing boards (as a crude measure ofsurplus for large-scale landowners/farmers) with savings data generated in a rural household budget survey of primarily small-scale farmers and landowners.[15] This measure, for reasons detailed in Appendix III, probably underestimates the wealth of the semi-arid pastoralist districts in northern and eastern Kenya.

In addition to the problems with the measure of wealth used, there is no reason to expect spending to be highly related to wealth because of the way in which county councils raise their revenues. Kenyan counties have not historically had general and consistent authority to tax wealth in their jurisdictions. The primary source of wealth in a local authority is land. As demonstrated earlier, some county councils get a great deal of revenue from land rates, while others get little. This is true not only because the value of land is low in some areas, but also because some places do not have the authority to levy such rates or because the rate they are allowed to charge by the Ministry of Local Government is very small. Some councils that do not have broad use of rates on land have been allowed to levy a cess

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[15] Livestock and agricultural sales information is available from the Ministry of Agriculture and the Ministry of Livestock Development, as well as from the marketing boards themselves. These include the Coffee Board of Kenya, the National Cereals and Produce Board, and the Kenya Meat Commission. The rural household budget survey was conducted by the Central Bureau of Statistics of the Ministry of Planning and National Development during 1981-82, but it has not yet been published.

on the value of crops grown on the land. However, the power to levy cess, until very recently, has been arbitrarily granted only to certain councils and only for certain crops. Two adjacent county councils growing basically the same crops were not always allowed to cess them at a uniform rate, or one of them might not be allowed any cess at all. Some councils, for example, were allowed to use coffee or maize cess, while others were not. Certain important crops that are the principal source of income generated in some districts, such as tea, were not cessed at all. Furthermore, a number of councils have little or no access to land rates, cess, or any other particularly productive sources of revenue. Given the inconsistent assignment and productivity of wealth-based taxes across councils, it is not surprising that wealth does not exert an influence on total spending.

Population density should not really be expected to have much of an impact on county council spending because it varies so greatly <u>within</u> county council areas. Thus, the population density for an entire jurisdiction may have little to do with the required pattern of service provision. Most county council services are concentrated in more urbanized areas and trading centers. The quality and levels of the various services also vary greatly across urban areas and trading centers. Much more disaggregate analysis would need to be done to see if density has an impact on spending levels in county councils, but the data required for this analysis are not available.

Having failed with the variables traditionally used to explain local authority spending, a variety of other variables were tested for their degree of association with per capita spending in county councils. Many of these were failures, but a few variables have emerged as being significantly related to the level of per capita spending. These are: per capita cess and land rates, per capita livestock, and per capita wage earnings.

The use of per capita cess and land rates as an explanatory variable may seem suspect, because they are principal sources of revenue in many county councils. Indeed, it is, at the very least, a partial identity: expenditures are made from revenues, so will obviously be strongly dependent on them. In this case, however, the point is that these sources of revenue are not consistently and uniformly available to all county councils, even though most councils have requested permission to use them. It would be expected that the councils that are allowed to use these productive sources and do raise substantial revenue from them are to a great extent the ones who are able to have higher per capita spending and provide a higher level of services. It is also interesting to note that there is virtually no correlation (.099) between per capita wealth and per capita revenue from cess and land rates. To some extent, this finding reflects problems with the measure of wealth. It also, however, strongly reflects the fact that some low wealth councils in northern and eastern Kenya get substantial income from miraa cess, while some councils with high agricultural potential get comparatively little or no money from cess or land rates.

Per capita livestock, the second significant variable used in the analysis of county council expenditure, reflects an important component of wealth, particularly in the northern and eastern semi-arid areas, which have little productive land, little agricultural activity, and with a few exceptions, insignificant access to land rates. Yet, these areas do raise revenue from markets, stock auction yards, slaughter houses and slabs, veterinary services, and a variety of other sources, many of which are livestock-related. Thus, this variable probably helps to explain some of the variation in spending in some of the more marginal districts of the country.

The final variable used in the analysis of county council expenditures is per capita wage earnings. Wage earners represent a small percentage of total employment in many counties, but they are a good reflection of income generated in the formal sector. Wage earnings can be expected to have multiplier effects in both the local formal and informal sectors, leading to greater local economic activity and boosting local authority taxes dependent on such activity.

The relationship between per capita spending and each of the three explanatory variables--per capita cess and land rates, per capita livestock, and per capita wage earnings--was found to be positive and significant. The pairwise correlations among the three variables are not significant, so they were all combined into the same regression equation, the results of which are presented in Table 5.2. All of the variables, as evidenced by the t-statistics, are highly significant, and together explain 81.7 percent of the variation in per capita spending across county councils.

Per capita livestock is the least significant of the explanatory variables. This is not surprising, as it primarily helps to explain spending in a small number of councils in which livestock activities are the primary economic activity. Per capita cess and land rates is the most significant variable, as would be expected. The lesson from this is very clear and bears repeating: those county councils having good access to cess and land rates are able to spend more on providing services to the residents of their jurisdictions. The Government of Kenya has recently taken an important step towards improving inequities in revenue generation and disparities in fiscal capacity across county councils by announcing its intention to make cess generally available to all county councils and allowing it to be levied

TABLE 5.2
REGRESSION 2 FOR PER CAPITA TOTAL EXPENDITURES IN COUNTY COUNCILS

Explanatory Variable	Coefficient	T-Statistic	Standard Error
Per Capita Livestock	1.1172	4.297	Ø.Ø26
Per Capita Wage Earnings	Ø.Ø1331	2.185	Ø.ØØ47278
Per Capita Cess and Land Rates	1.1889	5.Ø14	Ø.Ø23714

Intercept	: -5.862591
Coefficient of Determination (R-Square)	: Ø.863
Adjusted R-Square	: Ø.817
Multiple R	: Ø.929
Standard Error of Estimate	: 5.793

Correlation Coefficients for Explanatory Variables

Per Capita Livestock and Per Capita Wage Earnings	: Ø.Ø58
Per Capita Livestock and Per Capita Cess and Rates	:-Ø.117
Per Capita Wage Earnings and Per Capita Cess and Rates	: Ø.319

on a standardized set of crops.[16]

Municipal and Town Councils

Variations in the level of per capita spending in municipal and town councils are much easier to explain than they are in county councils. The traditional variables, population, per capita wealth, and population density, go a long way in explaining per capita spending in the urban areas.

Table 5.3 presents the results of a regression analysis using per capita expenditure in municipal councils as the dependent variable and population, per capita wealth, and density as the explanatory variables. Together these variables explain 90 percent of the variation in per capita spending. Wealth is by far the most significant variable at the .001 level of confidence. Density is also significant at a lower level, with population being substantially less significant.

It is interesting to note that wealth alone explains 78.3 percent of the variation in per capita total spending in municipal councils. When used individually as single explanatory variables, neither population nor density is very significant. Both of these variables become more significant when used in the same regression as wealth. The correlation

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[16] This will not, of course, help the county councils located in arid and semi-arid areas where few or no crops are grown.

TABLE 5.3
REGRESSION 3 FOR PER CAPITA TOTAL EXPENDITURES IN MUNICIPAL COUNCILS

Explanatory Variable	Coefficient	T-Statistic	Standard Error
Population	0.000375	1.173	0.00031974
Per Capita Wealth	0.018095	8.229	0.02199
Density	0.000141	2.738	0.00005134

Intercept	: 20.58066
Coefficient of Determination (R-Square)	: 0.933
Adjusted R-Square	: 0.900
Multiple R	: 0.966
Standard Error of Estimate	: 46.505

Correlation Coefficients for Explanatory Variables

Population and Per Capita Wealth	: 0.231
Population and Density	: 0.217
Per Capita Wealth and Density	: -0.151

coefficients among wealth, population, and density are low, indicating that multicollinearity should not be a problem. The conclusion must be that there is some type of moderate interactive effect among the three explanatory variables.

The results for municipal councils are exactly what would be expected. Wealth has been defined for municipal councils as per capita property valuation, and, as discussed earlier, property value is a good measure of economic activity in municipal councils. Municipal council revenue sources are much more closely related to wealth than are those of county councils, so it is clear why wealth exerts such a strong positive impact on per capita spending.

Higher population and density also exert some small positive influence on spending, but it is overshadowed by the effects of wealth. A higher level of services and a stronger revenue base tend to exist in some of the higher population councils, and it is reasonable for density to be associated with higher land values and higher spending in some cases. The interaction effect among the three explanatory variables probably comes from the fact that a few of the wealthiest municipal councils are also among the largest and most densely populated ones.

When looking at both municipal and town councils together, the same general relationships hold, but the significance of all of the explanatory variables declines, and the overall explanatory power of the regression is diminished. This is probably because two of the town councils have very high per capita land values. Their level of per capita spending, however, is well below that of the largest municipal councils, the other group with very high per capita land values. The town councils are not responsible for health and primary education, and generally they do not provide water and sewerage services. Thus, the strong positive relationship for municipal councils between per capita wealth and per capita expenditure is diminished by the inclusion of town councils.

Summary of Major Points Regarding Expenditure Determinants

Variations in per capita total spending in municipal councils are highly and positively related to variations in wealth (per capita property valuation). The wealthy councils tend to spend at a substantially higher per capita level than poorer councils. Size (population) and population density also have a moderate positive impact on per capita spending, but the former is less significant than the latter.

Variations in per capita total spending in county councils are almost completely unrelated to wealth. There is no tendency for wealthier county councils to spend at a higher per capita level than poorer county councils. This is true primarily because there is no consistent and standardized taxation of wealth across county councils, but there are also several peculiarities with the data that contribute to this situation.

The most significant factor affecting per capita total expenditures in county councils is per capita cess and land rates. The implication of this seemingly obvious finding is that county councils given significant access to these sources of revenue are able to spend more than other councils on service provision. These privileged councils are not necessarily the wealthiest ones.

Other factors significantly affecting per capita total spending in county councils are number of livestock per capita and per capita wage earnings. The former is a good measure of wealth, economic activity, and ability to raise public revenues in marginal pastoralist districts. The latter is a good measure of income generated in the local formal sector, which stimulates business in the local economy and generates additional revenue from business-based local taxes.

It is important to note that the analysis in this section focuses only on variations in per capita expenditure patterns across local authorities. These variations could be the result of differences in labor and other input costs, differences in the quality of service provision, and/or other factors. No attempt has been made to explain the importance of the various components of differences in per capita expenditures across councils, but some of them could be extremely important. For example, it is very likely that some of the expenditure differences may be due to differences in material and labor costs and productivity, implying that some councils may be more efficient providers of services than others. Labor costs for the councils visited for this study range from about 60 to more than 90 percent of total expenditures. Some of this difference is clearly attributable to differences in the service packages provided by different types of councils. Rural county councils, for example, provide only a very few labor-intensive services, such as social services and market-related services, so that their expenditures on labor will be high relative to other inputs regardless of differences in wages and productivity. Some councils, however, may well be able to get materials at lower cost and use less labor than they currently do to provide certain services.

Other Issues Related to Service Provision

Some of the major issues related to service provision, such as inadequate revenues and intergovernmental cooperation, will be analyzed in later sections of this and the next chapter. However, a few other issues regarding service provision should be briefly mentioned here.

Privatization of public services has not received much attention in Kenya. In some areas of the world, local governments contract with private firms to provide certain types of public services, such as refuse collection and facilities management. The rationale for privatization is that, even though it may involve some loss of public sector jobs, it may be more cost efficient than providing services directly by the public sector. There seems to be some interest on the part of certain local authorities in the possibility of hiring firms to perform particular services, such as refuse collection, and perhaps even to manage major facilities, such as slaughterhouses or markets. There are a few cases of minor private sector involvement in Kenyan local authorities in which private firms have increased revenue intake for the local authority while also earning a reasonable profit for themselves.

Nongovernmental organizations (NGOs) have a significant role to play in service provision in Kenya, particularly in the rural areas. Schools, health care, water, veterinary care, agricultural extension, and other basic services are all provided by NGOs. Although it is not possible to estimate the importance of NGO service provision in monetary terms, it is clear that the central government and local authorities rely on NGOs in many rural areas to provide services that the Kenyan public sector would otherwise find difficult or impossible to provide.

Finally, public service coverage within local authorities is often far from uniform across the entire jurisdiction. Sometimes this is justified on the basis of differing service needs, but it is more frequently nothing more than a manifestation of limited financial resources. Some local authorities do not have the capital or recurrent resources to extend certain services across all of the areas for which they are responsible.

Income Generation

The problem of income generation is unquestionably the most significant problem facing Kenyan local authorities. As shown in Chapter 4, there is tremendous diversity in the sources of revenue employed by local authorities, and many of them run substantial deficits on a regular basis. Part of the problem is that there is an inadequate revenue base, and part is due to serious intergovernmental, administrative, and political problems that seriously constrain the income generation process. This section will discuss public finance issues related to revenue generation, but a discussion of constraints will be reserved for the next chapter.

Inelasticity

One of the principal revenue problems for local authorities is the relative inelasticity of certain major components of their revenue bases with respect to income, prices, and population. Although there have not been formal studies to estimate elasticities, there is plenty of evidence to suggest that revenue inelasticity is a significant problem. Some important sources of revenue, such as land rates and house rents, are almost completely fixed for significant periods of time. Even though valuation rolls are supposed to be updated every five years, there are long delays in this process. Local authorities are permitted to impose interim rate increases between revaluations, but this is often difficult for political reasons, so that the revenue yield from land rates remains essentially static for five-year periods, except for small additions to the base from supplementary valuation rolls. Most local authorities do not employ their own valuer, so they rely on the Ministry of Lands and Settlement, which is not staffed to deal with the enormous workload in a timely fashion. Furthermore, valuation in Kenya is based on unimproved site value, so that the property tax base does not grow substantially with increases in local economic activity.

Other local taxes, such as market fees, are partially based on the level of economic activity, but they are almost always per unit rather than ad valorem charges, so that the revenue derived from the taxes grows slowly as the volume of trading grows. This problem is exacerbated by the failure of many local authorities to raise their per unit fees regularly as the cost of living goes up. If such taxes were indexed to the rate of inflation or based on the value of the product (e.g., 1% of the expected sales value of a bag of potatoes instead of three Kenyan shillings per bag), the revenue elasticity would be greatly enhanced. Of course, reasonably accurate price information would be required to institute indexing.

The inelasticity of local revenue sources creates serious problems for the local authorities. It essentially means that the growth of revenue is slower than the growth in costs and demand for services. Expenditure requirements may greatly increase with the growth of commercial activities and population, but revenue does not. As a result, some local authorities are faced with growing deficits each year, as noted in the previous chapter.

Instability/Overreliance

Some local authority revenue sources, such as house rents, do not grow regularly or rapidly over time, but are rather stable. Others sources of revenues, however, are much more unstable. Market and stock auction fees, for example, are dependent on the level of trading. Thus, in years when there is a crop failure or low animal sales because of drought or disease, the volume of revenue can be substantially reduced. This is especially a problem in semi-arid areas where the arrival of rain is uncertain. It could also, however, be a problem even in relatively wealthy agricultural areas at certain times because of the extreme dependence of some local authorities on one or two main sources of revenue. Some of the county councils who are permitted to charge agricultural cess, for example, are so dependent on cess revenue that a serious crop failure could possibly render them insolvent. Some local authorities may get 40 or 50 percent of their annual income from coffee or miraa cess.

The problem of local government revenue instability is clearly demonstrated by the data in Table 5.4. There was a serious drought in Kenya in 1984 during which agricultural production fell by 3.7 percent from the previous year and gross domestic product increased by only 0.9 percent. This did not affect the growth trend of central government recurrent revenues and expenditures greatly. In spite of the downturn in economic activity, revenues rose by 10.4 percent between 1983 and 1984, from 923.62 to 1019.59 million pounds, while expenditures rose by 10.8 percent, from 984.58 to 1091.32 million pounds. During the same time period, the local authority revenue base was greatly eroded. Municipal council revenues fell by 11.1 percent, from 52.73 to 46.89 million pounds, and expenditures fell by 19.0 percent, from 50.55 to 40.93 million pounds. Other local authorities, primarily county councils with jurisdiction over rural areas, were even more dramatically affected. Their income fell by 36.2 percent, from 12.94 to 8.26 million pounds, while expenditures declined by 38.6 percent, from 11.6 to 7.16 million pounds. In all cases, local authority revenue and expenditure increased in 1985 as the country recovered from the drought.

TABLE 5.4

RECURRENT PUBLIC EXPENDITURES AND REVENUES, 1982-86
BY LEVEL OF GOVERNMENT (MILLIONS OF KENYAN POUNDS)

LEVEL OF GOVERNMENT	1982	1983	1984	1985	1986*
			EXPENDITURES		
Central	861.40	984.58	1091.32	1244.26	1551.62
Municipal Councils	46.99	50.55	40.93	52.67	46.06
Other Local Authorities**	11.07	11.66	7.16	12.76	5.41
			REVENUES		
Central	832.17	923.62	1019.59	1186.36	1477.50
Municipal Councils	51.19	52.73	46.89	56.74	55.69
Other Local Authorities	13.15	12.94	8.26	12.69	15.38

*The figures for 1986 are provisional and should not be considered accurate, particularly for the local authorities. This is true because there are extensive delays in the issuing of local authority financial figures on account of slow auditing procedures and administrative delays on the part of local authorities and the Ministry of Local Government. It is highly unlikely that local authority revenues actually went down as the figures suggest. The Kenyan economy had a good year in 1986. Real value-added in the manufacturing sector grew by 5.9 percent, the agricultural sector grew by 4.8 percent, and real gross domestic product rose by 5.7 percent.

**Town, urban, and county councils.

SOURCE: Economic Survey, 1987 (Nairobi: Central Bureau of Statistics, Ministry of Planning and National Development, Republic of Kenya, 1987), Chapter 6.

In general, there is too much dependence of Kenyan local authorities, particularly county councils, on sources of revenue that are not stable and reliable. Furthermore, in some cases, there is far too much reliance on only one or two sources of revenue that are subject to forces beyond the control of local authorities.

Efficiency

Largely because of the diversity and inconsistency of the revenue base, local authority taxes in Kenya are not often very general in coverage. In some municipal councils, there is, in fact, fairly general coverage of most economic activities through a system of land rates, business and trading licenses, and marketing and vending fees. In other urban and most rural areas, tax system coverage is much less general. In a few county councils, there are agricultural land rates or cesses in the rural areas and land rates and trading fees in the urban areas. However, many of the county councils with agricultural land and/or production taxation do not bother much with taxes in their urban centers, while those who do not have agricultural taxes tend to tax very heavily in their urban centers.

The diversity and lack of generality of the local authority tax base certainly creates the possibility of serious efficiency effects, but it is very difficult to measure them. There are significant interjurisdictional differences in both the local tax base and local tax rates that could generate locational efficiency effects. This is not very likely, however, for several reasons. First, there are clear cultural constraints on mobility in Kenya. Many people will not want to give up their residence or business in their home area even if taxes are higher than in other areas. Of course, this is not to say that large-scale industrial investors will not, to some extent, react to interjurisdictional tax differences, but most large-scale industry in concentrated in a few large urban centers in Kenya, and there are needed inputs and local business tax incentives in these places. Second, the absolute levels of most local tax rates and charges in Kenya are fairly low, and it is likely that many people would not respond even to relatively large interjurisdictional tax differences, particularly if there were other more important considerations, such as access to labor or nearness to family.[17] Third, information about tax differences in other districts is probably not widespread. It will be shown later, for example, that there are enormous differences in

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[17] The Institute for Development Studies at the University of Nairobi has just completed a detailed study of the informal sector in four districts in Kenya. The results of the study clearly show that, although informal sector workers complain about license fees and taxes, only three percent of the respondents in the survey indicated that license fees and taxes were a barrier to them in setting up their businesses. Details may be found in Ng'ethe, Wahome and Ndua (1987).

business license fees and land taxes between local authorities in the same district or contiguous districts, yet there is no clear evidence of a migration to the less expensive area. Finally, many producers in Kenya must operate in a particular region because of the nature of their business. A coffee grower must operate in a particular agro-ecological zone. He/She is not in a position to move to a semi-arid district even if it has lower agricultural or land taxes than a district that has good coffee land. Although food crops might be grown in the semi-arid district, the after-tax return from coffee or other cash crops is likely to be much higher.

The possibility of intrajurisdictional efficiency effects is somewhat greater than in the interjurisdictional case. For example, there are sometimes great differences in the cess rate charged on different agricultural crops in the same district. This may induce a farmer to shift to the less highly taxed crop if the after-tax return is higher. However, this is probably not common. Higher cesses are normally on higher-value crops, so the after-tax return on the more highly taxed crops may still leave the farmer indifferent or better off. Similarly, sometimes not all sections of an urban area are surveyed and valued, and there are no land rates charged in unsurveyed areas. This may induce some businesses and residents to move to unsurveyed sections of the urban area. It is also doubtful that this is widespread, but there are certainly some cases of it in Kenya.

Equity

It is difficult to assess adequately the equity of local authority revenue sources in Kenya because of a lack of relevant data, but it is possible to make a few observations. First, it is clear that there is little equity across local authorities. The fact that some farmers have to pay cess and others do not is certainly not equitable, nor is the fact that the same taxes are charged at such different rates in similar local authorities.

There are also clearly some vertical and horizontal inequities within local authorities. A local authority with stock auction and market fees but no cess or agricultural land rates might be a case in point. In this example, small farmers or herders who sell one bag of potatoes or one cow locally in the period of a week will have to pay fees to the local authority, but a wealthy farmer who may cultivate thousands of acres may pay little or nothing.

In many local authorities, most of the major tax revenue comes from center city merchants and businessmen. They often have to pay land rates or rents, fees and charges for water, sewerage and conservancy, and license fees. Although they may be among the wealthiest people in the jurisdiction, some of their middle and higher income counterparts who are less centrally located or located in unsurveyed parts of the city center may be much less heavily taxed. In general, only businesses are taxed to any significant degree in many local authorities, and some of them are treated very differently from others.

Another potential equity issue is relevant in county councils where there are great differences in agro-ecological conditions and economic activity in different parts of the counties. In a county such as Meru, for example, the landscape ranges from productive, wealthy agricultural divisions near Mt. Kenya, where coffee is cultivated, to semi-arid areas in which little can be grown, with many people relying on subsistence herding for their existence. In such cases, fees, charges, and taxes are usually uniform across the entire jurisdiction, despite the tremendous divisional differences in ability-to-pay.

Thus, there is no general statement that can be made regarding the horizontal, vertical, and geographical equity of local authority taxes in Kenya. There are clearly equity problems, but their nature and severity differs widely across local authorities.

Other Revenue-Generation Issues

The data presented earlier in Table 4.2 clearly demonstrate that many local authorities in Kenya exploit entrepreneurial revenue-raising activities, at least to some extent. Virtually all local authorities build and operate marketplaces, and many provide livestock slaughter facilities (houses and slabs), housing, and busparks as well. In some cases, these activities provide a significant proportion of revenue for local authorities. This is particularly true for rural local authorities who may have few other good sources of revenue. In many cases, these revenue-raising activities involve services that could be, but are unlikely to be, provided by the public sector.

A final important point regarding local authority revenue is that Harambee (self-help) projects raise a great deal of money in Kenya to assist in the provision of public services, some of which would otherwise have to be financed by local authorities.[18] People voluntarily contribute large sums of money, labor, and materials over and above central and local government taxes towards community projects that are often undertaken independently of local authorities.[19] Most of these contributions are used for the construction costs of capital investment projects. The education sector, which is primarily funded by the central government, is the major beneficiary of Harambee, but fund-raising events are sometimes held for local government services. Community

[18] Harambee was the name for the self-help movement in Kenya coined by the late Mzee Jomo Kenyatta.

[19] Barkan and Holmquist (1986) conducted a survey of Harambee contributors, the results of which suggest that Harambee can be considered, at least in some areas, a progressive form of voluntary local taxation.

centers, water supply projects, markets, cattle dips, and other facilities and services have benefitted significantly from Harambee. In 1985, over 37 million Kenyan pounds (about US $45 million), both cash and in-kind, were donated to Harambee projects, a sum about twice as great as total local authority gross fixed capital formation in the same year. Large-scale Harambee projects, however, tend to occur primarily in the areas where people can afford to donate. The poor districts in arid or semi-arid regions rarely, if ever, have significant Harambee projects.

Some observers of Harambee have noted that it has become very controlled by the central government over the years and cannot be truly considered local self-help.[20] The government controls Harambee activities by licensing fundraising activities and requiring approval of such activities by district officials. Furthermore, local Harambees are often hosted by prominent national politicians who use the occasions to further their own political interests.

Revenue-Expenditure Linkages

The issue of revenue-expenditure linkages is a very

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[20] Central government control of Harambee is discussed extensively in Colebatch (1974). More recently, Ngau (1987) has argued that central government interference has biased the nature of Harambee projects towards large, costly social amenity projects, and has undermined the degree of broad-based participation in making project selections.

complex one in the Kenyan case, and the situation varies greatly across local authorities.[21] Because most services are not assigned by the central government per se and most sources of revenue are allowed to all local authorities provided the proper clearances are obtained, it does not, on the surface, seem that there should be difficulties in obtaining a correspondence between service provision and sources of income. Unfortunately, the situation is not nearly that simple.

Most municipal councils provide traditional urban services. Many of these services can be financed by charges if the charge levels are properly set and the revenue is actually collected. Land rate and license income should go a long way towards covering the costs of most services for which charges cannot be made. Some of the largest municipal councils have additional responsibilities for health and education, but the latter is largely financed financially by generous grants for teachers salaries from the Ministry of Education. Health is the one service where significant problems might be foreseen because of an inability to charge fees and a lack of aid from the central government. In general, however, there seems to be a fairly good correspondence between services provided by municipal

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[21] The principal discussion of intergovernmental grants, an important revenue-expenditure linkage issue, is presented in the next chapter under the treatment of intergovernmental institutional issues.

councils and their sources of income. Unfortunately, this correspondence breaks down because of institutional, managerial, and political constraints, which will be discussed in the next chapter.

In the rural councils, the correspondence between expenditures and income is much less apparent. There are few fee-for-service type activities in many county councils, and some of the major ones, such as water and veterinary services, often require subsidies. Furthermore, local authorities in urban areas all have access to land rates, but there is no general and productive source of revenue available to all county councils except license fees. As shown earlier, some county councils have land rates, others have agricultural cess, a few have both, and still others have neither. The situation is further complicated for county councils by the same institutional, managerial, and political constraints that plague municipal councils.

Even in the case where an revenue-expenditure correspondence seems to exist, there is no guarantee that sufficient revenue will be raised to cover the costs of service provision. Tax rates, fees, and charges must be set on a reasonable and rational basis in order for adequate income to be raised, and this is not often the case in Kenyan local authorities. The rest of this section will deal largely with issues related to cost recovery and setting the levels of fees and taxes.

Cost Recovery

Poor cost recovery from service provision is a serious problem in many Kenyan local authorities. Tables 5.5 and 5.6 present some basic information on the number of councils examined in this study who ran surpluses and deficits on the provision of particular services in 1984. Note that not all councils provide all of the services listed in these tables. Furthermore, in several cases, it was not possible to get the information for a few services for some of the local authorities being studied.

County councils do not do very well financially with most of the services they provide. The data in Table 5.5 indicate that only four of eleven county councils ran surpluses for markets in 1984 and only three of five ran surpluses for slaughterhouses. Few county councils run surpluses on housing (two of four), water services (one of six) or sewerage (zero of two).

Certain other services also seem to be financially disastrous for many or most county councils. Only two of eight councils generate surpluses on veterinary services, with similar or more dismal records for social services (zero of thirteen), works (one of eight), and conservancy (one of five). Only tourism, for which four of five county councils earn surpluses, seems to be a promising source of surplus revenue. The one case of a deficit is for a remote council

TABLE 5.5
SURPLUS/DEFICIT OF SPECIFIC SERVICES IN SELECTED COUNTY COUNCILS* (1984)

Service	Number of Surpluses	Number of Deficits
Conservancy	1	5
Housing	2	2
Markets	4	7
Sewerage	Ø	2
Slaughter	3	2
Social Services	Ø	13
Tourism	4	1
Veterinary	2	8
Water	1	5
Works	1	8

TABLE 5.6

SURPLUS/DEFICIT OF SPECIFIC SERVICES IN SELECTED MUNICIPAL AND TOWN COUNCILS* (1984)

Service	Number of Surpluses	Number of Deficits
Conservancy	2	4
Housing	8	2
Markets	8	5
Sewerage	5	4
Slaughter	6	6
Social Services	Ø	13
Veterinary	Ø	2
Water	6	2
Works	Ø	13

*There were 13 county and 13 municipal and town councils included in this study. The sum of surpluses and deficits does not always add to the total number of local auhorities. Not all councils provide all of the listed services. In addition, in a few cases, finanical records were not sufficiently disaggregate to allow the extraction of data for particular services.

whose only tourist activity is an unprofitable guest house.

It could be argued that some of these services should be subsidized by county councils, and some by their nature are not revenue-generating activities. It is not reasonable, for example, for a council to expect to make revenue from works services. This basically involves the provision of roads and street cleaning, with only minor sources of revenue, such as planning fees, plot allocation fees, and revenue from equipment rental. It is also clear that local governments might be expected to subsidize social services (primarily nursery schools) and veterinary services because of the externalities they generate.

Other types of services, however, such as housing, water, sewerage, markets, slaughter, and conservancy, are essentially fee-for-service activities. The local authorities should, to as great an extent as possible, charge fees that reflect the costs of service provision. In some very poor areas where people truly cannot afford to pay for basic services, a case can be made for Government of Kenya subsidization through grants to needy councils or ministerial assumption of responsibility for providing certain services. With very few exceptions, the county councils that do tend to generate surpluses on some services are those located in high potential agricultural areas, such as the Kipsigis, Nakuru and Wareng County Councils.

Municipal and town councils are more likely to generate surpluses on specific services than are county councils, as can be seen in the data presented in Table 5.6. The poorest performance is primarily in those services for which subsidization would be expected. All 13 councils run deficits for the provision of works and social services, and both of the councils providing veterinary services run deficits.

Some of the services that would be expected to be profitable, in fact, generally are: eight of ten councils run surpluses for housing services and six of eight do for water provision. It is worth noting that the housing deficits are incurred in Nakuru and Eldoret, two of the largest municipal councils in Kenya. This is a disturbing sign, particularly because both have very large housing schemes and housing is one of the services that has historically provided surplus revenue to cover deficits on general funds in large municipal councils. Now, water and sewerage seem to be saving the day in these particular councils.

It is also disturbing that certain services that should cover costs through fees do not do so in a substantial number of municipal and town councils. Only five of nine councils generate a surplus for sewerage and only eight of thirteen do so for markets, which are a source of enormous surplus in some other councils. Similarly, only six of twelve councils have a surplus for slaughterhouses and only two of four for conservancy services.

Deficits on water and sewerage seem to be experienced primarily in a few of the smaller and/or less-developed councils, such as Bungoma, Kisii, Muranga, and Karatina. This is not true of the councils who have deficits for conservancy, markets, and slaughterhouses. These councils range from some of the largest (Nakuru, Kisumu and Eldoret) to some of the smallest (Kitui, Busia and Karatina, all of which are town councils). Most of these councils run deficits on only one or two of these services.

Discussions with local authority officers, observation of revenue collection procedures, and examination of local authority financial records suggest that there are three primary reasons why councils run deficits on services that should be profitable. First of all, in some councils, fees are set too low to cover the actual cost of services. Sometimes this occurs because of local political pressures, but sometimes it is nothing more than a matter of poor planning and management. Second, costs for some services are extremely high due to poor productivity, and/or a supply of workers larger than what is necessary to provide the services, and/or salary increases imposed by the Public Service Commission or the Industrial Court. Efficiency can clearly be improved in many cases, while in others the fees for service provision need to be raised to match the necessary costs. Finally, revenue collection and enforcement are extremely lacking for some or all services in many councils. This situation results from a combination of factors: insufficient and/or poorly trained staff, corruption, inadequate collection and enforcement procedures, insufficient enforcement authority, and interference from local politicians. All of these collection issues will be discussed further in the next chapter.

Setting Fees and Taxes[22]

There are no established guidelines for setting tax rates and user charges in local authorities in Kenya. Service charges, land tax rates, and license fees vary dramatically across local authorities, and there seems to be little rational basis for these differences. Part of the blame for this situation lies with the local authorities, who have no system or guidelines for setting tax rates and charges. The Ministry of Local Government, which is required to approve all rates and charges levied by the local authorities, must also share the blame. The Ministry does not have guidelines for approving rate and charge requests from the local authorities, so that many of these decisions are arbitrary and open to political manipulation.

There is some clear evidence to demonstrate the lack of uniformity in fees and taxes across local authorities.[23]

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[22] Issues related to setting fees, charges, and taxes in Kenya are discussed in greater depth in Smoke (February 1987).

[23] The only ad valorem tax collected by most local authorities is land rates, which vary from a two percent to

Tables 5.7 through 5.9 present selected summary data on the level of license fees and user charges in county, municipal and town councils. Mean fee and charges across different types of local authorities generally follow an expected pattern. For the most part, the fees and charges of municipal councils are substantially higher than those of county councils, while those of the town councils are somewhere in between. There are a few exceptions to these general trends, but they are rare.

The fees and charges levied by a particular type of council, on the other hand, vary dramatically across local authorities. It is not unusual, for example, for two county councils with similar characteristics to charge very different fees for the same license or service. Although there are sometimes rational explanations for these variations, many of the differences seem arbitrary, with no apparent justification on the basis of population, wealth, or costs of service provision.

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more than a ten percent actual tax rate. They are not dealt with here because of problems in interpreting the differences in land rates across local authorities. Almost all land valuation is done by the Ministry of Lands and Settlement in Kenya, and they are sometimes years behind schedule in doing local authority valuations, which are required every five years by law. In years between valuations, local authorities are permitted to raise their land tax rates annually, an option that some take advantage of but most do not. Diverse rates are levied on bases valued at various percentages of market value. There is no measure of equalized valuation, so that it is not possible to derive effective tax rates. Thus, it is not possible to compare land tax rates across local authorities in any meaningful way.

TABLE 5.7
COUNTY COUNCILS FEES AND CHARGES
SELECTED SUMMARY STATISTICS
(in Kenyan Shillings)

	DESCRIPTIVE STATISTICS				
FEE/CHARGE	Number	Mean	Median	Maximum	Minimum
A. LICENSE FEES					
RETAIL					
Bakery	13	585	350	1,550	200
Butchery	13	375	300	650	150
Chemist	3	483	500	750	200
Grocer	13	212	200	400	50
Hides/skins	11	567	400	2,000	100
SERVICES					
Bar License (on)	10	528	450	1,000	375
Bar License (off)	10	365	350	500	200
Barber	12	165	200	275	50
Garage	12	1,033	875	2,000	400
Hotel (maximum)	13	1,510	1,000	5,000	200
Petrol Station	13	973	1,000	2,500	300
Shoe Repair	10	192	200	400	100
OTHER					
Auctioneer	9	1,472	1,000	5,000	300
Stock Trader	9	653	300	2,000	250
Wholesale (Local)	12	983	675	2,500	400
Wholesale (Travel)	7	1,979	2,000	3,750	600

TABLE 5.7 (CONTINUED)

FEE/CHARGE	DESCRIPTIVE STATISTICS				
	Number	Mean	Median	Maximum	Minimum
B. USER CHARGES					
Bus Park Fees	7	These vary a great deal across councils that use them. Some councils charge annual fees while others charge on a per trip basis.			
Conservancy (annual)	9	131	100	240	50
Market Fees	13	Charges are usually levied per bag/bundle of goods to be sold and vary by type of product. Such charges are generally small, c. 1 to 15 K.Sh., and are fairly comparable across county councils.			
Slaughter Fees					
- cattle	10	18	15	40	5
- smallstock	10	7	7	15	2
Stock Auction					
- cattle	10	15	15	40	5
- smallstock	10	6	5	10	2

TABLE 5.8
MUNICIPAL COUNCILS FEES AND CHARGES
SELECTED SUMMARY STATISTICS
(in Kenyan Shillings)

	DESCRIPTIVE STATISTICS				
FEE/CHARGE	Number	Mean	Median	Maximum	Minimum
A. LICENSE FEES					
RETAIL					
Bakery (Lg)	9	2,016	2,500	3,500	500
Bakery (Sm)	9	1,488	1,500	3,500	400
Butchery (Lg)	10	1,100	800	2,500	400
Butchery (Sm)	10	665	725	1,000	300
Chemist	10	4,106	3,000	5,000	700
Grocer	8	494	550	1,000	300
Supermarket	9	2,832	2,560	4,500	1,350
Hides/skins	9	1,810	1,500	4,000	200
SERVICES					
Bar License (on)	9	925	900	1,500	400
Bar License (off)	9	453	400	700	300
Barber	10	317	300	550	100
Garage (enclosed)	10	2,313	1,990	4,500	600
Garage (open-air)	10	800	600	1,500	500
Hotel (residential)	10	1,032	850	2,000	300
Hotel (tourist)	10	3,465	3,500	5,500	1,000
Petrol Station (fuel only)	10	2,315	2,125	5,250	600
Petrol Station (fuel/repairs)	10	3,215	3,500	5,250	1,000
Shoe Repair	10	196	180	400	100

TABLE 5.8 (CONTINUED)

FEE/CHARGE	DESCRIPTIVE STATISTICS				
	Number	Mean	Median	Maximum	Minimum
OTHER					
Auctioneer	7	2,136	2,250	4,000	1,000
Stock Trader	3	467	500	800	100
Wholesale (local)	10	2,045	2,000	4,620	600
Wholesale (travel)	6	1,773	1,625	3,000	750
B. USER CHARGES					
Bus Park Fees (per trip)					
- bus	8	9/67	10	15	7/50
- matatu	8	4/13	5	6	2
Conservancy*	10	17	15	30	7/50
Market Fees	10	Charges are usually levied per bag/bundle of goods to be sold and vary by type of product. Such charges are generally small, c. 1 to 15 K.Sh., and are fairly comparable across municipal councils.			
Nursery**	6	283	150	840	80
Sewerage*** (monthly minimum)	7	20	14	45	9
Slaughter - cattle	9	77	80	150	35
- smallstock	9	27	30	30	15
Water*** (monthly minimum)	6	27	25	60	10

* monthly charge
** annual charge
*** charges for water and sewerage vary with volume of use in all cases.

TABLE 5.9
TOWN COUNCIL FEES AND CHARGES
SELECTED SUMMARY STATISTICS
(in Kenyan Shillings)

FEE/CHARGE	DESCRIPTIVE STATISTICS				
	Number	Mean	Median	Maximum	Minimum
A. LICENSE FEES					
RETAIL					
Bakery	3	1,167	1,000	1,500	1,000
Butchery	3	833	500	1,500	500
Chemist	2	1,100	1,800	400	1,100
Grocer	3	733	300	1,500	200
Hides/skins	2	450	450	500	400
SERVICES					
Bar License (on)	3	650	700	750	500
Bar License (off)	3	367	400	500	200
Barber	3	307	300	500	120
Garage (enclosed)	3	1,267	1,000	1,800	1,000
Garage (open-air)	3	617	500	850	500
Hotel (residential)	3	567	700	800	200
Hotel (tourist)	3	1,467	1,500	2,500	400
Petrol Station	3	1,833	1,500	2,000	1,500
Shoe Repair	3	233	200	300	200
OTHER					
Auctioneer	3	1,600	1,500	1,800	1,500
Stock Trader	3	600	300	1,200	300
Wholesale	3	1,800	1,200	3,500	700

TABLE 5.9 (CONTINUED)

FEE/CHARGE	DESCRIPTIVE STATISTICS				
	Number	Mean	Median	Maximum	Minimum
B. USER CHARGES					
Bus Park Fees (per trip)					
- bus	3	13	15	15	10
- minibus	3	8	10	10	5
- matatu	3	5	5	7/50	3
Conservancy (annual)	3	110	100	240	100
Market Fees	3	Charges are usually levied per bag/bundle of goods to be sold and vary by type of product. Such charges are generally small, c. 1 to 15 K.Sh., and are fairly comparable across town councils.			
Slaughter					
- cattle	2	50	50	60	40
- smallstock	2	17/50	17/50	20	15

The major reason for the existence of these variations is probably the lack of standards for setting fees and taxes both at the local level and within the Ministry of Local Government. Some local authority officers undoubtedly look at the fee and tax levels of other local authorities and service costs when setting their own fees, but many are unable to provide a reasonable explanation of how they set their rates. The Ministry has no guidelines and criteria for making decisions about local authority requests for approval of fees and charges and no basis for making comparisons across councils.

Another important factor in explaining the differences in the levels of fees and charges across local authorities may be the differential access that councils have to other sources of revenue. Some of the county councils in wealthier agricultural areas or municipal councils with water systems and housing estates may not need to charge high license fees because they have access to far more productive sources of income, which may also be less troublesome to collect. Muranga County Council, for example, gets a great deal of revenue from coffee cess, and Wareng County Council has extensive and productive land rates. Some of the poorer county councils in semi-arid districts, such as Turkana and Marsabit, have no access to such productive sources of revenue and thus end up charging higher fees than their wealthier counterparts for many types of licenses. There is a possibility that the lower fees in wealthy areas further encourage business, while the higher fees in poor areas may discourage it, but this is difficult to verify empirically because of a lack of relevant data.

The degree to which local authorities make distinctions in fee and charge levels on the basis of location, size, and other business characteristics varies greatly. All of the councils make some license fee distinctions between wholesale and retail traders, but most make few other distinctions on the basis of scale of operation. A few differentiate on the basis of such factors as: sidewalk versus shop traders and service providers; mechanized versus manually-operated equipment; lodging house capacity; and, snack bar versus restaurant versus restaurant/bar.

Few of the local authorities studied make fee and charge distinctions on the basis of location. Several county councils, however, do have different fees and charges for urban centers and rural areas. A handful of the municipal councils charge different fees in different areas of the city or distinguish between the town center and its extended area.

Most local authorities have between 100 and 200 different types of charges, with fees varying dramatically across different types of professions and trades. Although some of these distinctions are very important and easily justified, many of them cannot be considered very meaningful. For example, Embu Municipal Council charges an annual fee of

2550 Kenyan shillings (K.Sh.) for a bakery license, while its fee for a butchery license is only 750 K.Sh. Local officials are not able to justify this distinction. Do bakers generally earn more than three times as much income as butchers, or is it that they use more local authority services? The fee structure does not seem to be justifiable on rational grounds.

A related issue is the degree to which local authorities actually collect revenue from the license fees they have on their books. Most local authorities have many different types of fees listed in their schedule of fees and charges, but how many of these fees actually provide revenue? Unfortunately, this information is often difficult or impossible to get due to the way local authority records are kept. There are, however, a few bits of information indicating that local authorities may, in some cases, collect revenue from only a limited number of fees. Wareng County Council, for example, collected revenue from only 61 of the 116 fees listed in its schedule of fees and charges (52 percent) in 1984. A more dramatic case is Turkana County Council, which recently collected revenue from only 28 of the 108 fees on its schedule (26 percent). The fact that little or no revenue is generated from many gazetted fees may help to explain why local authorities tend to take little systematic care in setting fee levels.

Recovery of Revenue from Nonresidents

A serious revenue problem faced by some municipal councils is the fact that there is no mechanism for local authorities to recover revenue from residents of other local authorities who use some of their services. This is not true, for example, of nonresidents who use the local bus park or sell in the local market, but it can be a serious problem for such services as health care, and to a lesser extent, education, which are provided by some of the larger municipal councils. Municipal hospitals, for example, may be better-staffed and better-supplied than district hospitals, so that people may have to wait less time and will be more likely to be able to get needed drugs. Thus, some residents of the county council's jurisdiction come to the municipal hospital for their health care requirements. Because health care is free in Kenya by Presidential decree, the municipal council cannot charge for these services, and there is no mechanism for recouping this revenue either from the county council or the Ministry of Health. This can create a serious burden on the municipal council, and it means that residents of the municipal council are subsidizing the residents of other jurisdictions.

This problem of revenue recovery is a lesser problem with some other general local authority services. Nonresidents who come into a local authority benefit from the local roads, street lights, sanitation, conservancy services, etc., but do not contribute to the costs of providing these services in any meaningful way.

Summary of Public Finance Issues

The pattern of service provision that has emerged in Kenyan local authorities is, to a great extent, justifiable on the basis of the criteria outlined in Chapter 3. There are a few ambiguities in the assignment of certain services, such as water supply and veterinary care, and a case could be made for greater decentralization of responsibility for education. For the most part, however, a majority of "local" services are provided locally, and the central government does intervene in the provision of services that involve economies of scale and externalities. There are problems with arrangements for intergovernmental and interagency coordination of service provision, but a discussion of this is reserved until institutional issues are discussed in the following chapter.

On the revenue side, efficiency effects generated by local taxes are not likely to be severe except in particular cases. In addition, many local authorities augment their revenues by exploiting entrepreneurial revenue-raising activities, and Harambee and nongovernmental organizations supply funds for certain facilities and services that would otherwise have to be provided by local authorities.

In spite of these positive aspects of the local public finance system, there are significant problems with local authority revenue generation in Kenya. There are substantial horizontal and vertical inequities in local tax systems both within and across local authorities. More importantly, the task of local service provision is often seriously undermined by the inelasticity or instability of many local revenue sources. Finally, the central government is frequently arbitrary in granting local governments the authority to use particular sources of revenue, a practice that generates artificial fiscal disparities across local authorities.

There are also serious deficiencies in the correspondence between revenue-raising authority/capacity and expenditure responsibility in Kenyan local authorities. It would appear that the correspondence between revenues and expenditures should be adequate for municipal councils. In reality, there are major problems, largely due to institutional and procedural weaknesses to be discussed in Chapter 6. The situation is much worse for county councils, where there is often little correspondence between revenues and expenditures. There are no guidelines and procedures for setting local fees, charges, and tax rates, and cost recovery is a serious problem in many local authorities.

It is evident that the revenue side presents the major deficiencies and problems with local public finance in Kenya. Both the revenue and expenditure sides, however, are seriously affected by problems with the institutional organization and capacity of the Kenyan public sector. The next chapter turns to an examination of these institutional issues and the impact they have on local government finance in Kenya.

CHAPTER 6

ANALYSIS AND EVALUATION OF THE FISCAL ROLE OF LOCAL GOVERNMENT IN KENYA, PART II: INSTITUTIONAL ISSUES

A variety of problems related to institutional organization, capacity, and procedures have imposed major constraints on the fiscal performance of Kenyan local authorities. Many of these institutional issues are intergovernmental in nature, while others relate primarily to the local authorities. This chapter examines major institutional problems that affect the fiscal role of local authorities in Kenya and their ability to provide public services.

Intergovernmental Issues

In any multitiered government system, intergovernmental institutional arrangements are an important determinant of the quality of public service provision. Some of the existing intergovernmental relationships and procedures in Kenya, however, constrain rather than facilitate local authority performance in meeting local service needs. Other relationships and procedures that could be productive for local authorities do not exist, or are poorly conceived and implemented. This section will examine the most important of these intergovernmental institutional issues, including interjurisdictional coordination of local authorities, central government monitoring and control, intergovernmental grants, local authority capital financing, and the relationship between local authorities and other public sector institutions.

Interjurisdictional Coordination of Local Authorities

Interjurisdictional cooperation among local authorities is very rare in Kenya. The Local Government Act does provide for the formation of joint committees and joint boards across local authorities for the planning and provision of mutually beneficial projects subject to the approval of the Ministry of Local Government. However, not one of the local authorities visited or officials interviewed for this study could provide a single example of interjurisdictional cooperation. There have been cases observed for this research in which such cooperation would have been very appropriate. For example, a municipal council putting in a water line to serve part of its constituency was to pass its line through villages under the jurisdiction of the county council. Water service was also being planned for the county council villages, although it was not scheduled to be implemented right away. Nevertheless, it would certainly have been more cost-effective for both the county and municipal councils if they had coordinated their efforts rather than each undertaking a fully separate project, but it is clear that they will end up taking the latter route.

Various forms of intergovernmental cooperation at the local level are widely used in countries with developed local government systems. The local authorities in Kenya seem not to realize the potential benefits of coordination, and they have no precedent or encouragement from the central government to arrange joint undertakings that increase efficiency.

The one genuine form of intergovernmental cooperation in Kenya--the regional development authority--is too new to evaluate, and it is limited in its geographical coverage. In 1980, the Government established three regional development authorities: the Lake Basin Development Authority, the Tana and Athi Rivers Development Authority, and the Kerio Valley Development Authority. Each covers at least several districts. Their primary goal is to manage and plan activities related to hydrological resources within their jurisdiction, but they are also supposed to monitor, coordinate, and evaluate all development activities undertaken in their areas. Although there have not been many major accomplishments yet, there is certainly potential for valuable projects and activities that might be undertaken by these regional authorities. However, their relationship to other levels of government and agencies is not very clear, and this ambiguity may constrain their ability to provide effective coordination.

Central Government Monitoring and Control of Local Authorities by the Ministry of Local Government

The central government in Kenya has a major role to play in monitoring and supporting the service provision activities of local authorities. This may be considered necessary, at least to a certain extent, because of widespread limitations in local authority capacity. It is clear, however. that the type and degree of control over local authorities currently exercised by the central government is neither justifiable nor productive. This inefficient control has remained in place for a variety of reasons, some of which are related to bureaucratic inertia and resource constraints. The primary reason, however, is probably political. The history of local government in post-independence Kenya, as discussed in Chapter 4, suggests that strong central government control of local authorities has been motivated more by politicians who desire to keep the local authorities dependent and weak than by a concern for their operating efficiency.

The major agent for central government control of local authorities in Kenya is the Ministry of Local Government (MLG), which supervises the functioning of all local authorities in Kenya. Under the Local Government Act, the Minister for Local Government has broad powers of control over local authority activities. Annual budget estimates, employment requests, by-laws, and schedules of fees and charges must all be submitted to the MLG for review and approval. The Ministry also reviews capital spending plans, approves loan requests, and processes requests for raising additional revenue. Thus, all major activities of local authorities are subject to MLG review and control. Some of the ways in which MLG exercises its control, however, generate a variety of significant problems. The information in this section on problems in the relationship between MLG and local authorities comes from personal observations as well as extensive interviews with local authority and Ministry of Local Government officials.

Excessive Control/Centralization

Among the local authority officials and Provincial Local Government Officers (PLGOs) interviewed for this study, there was no general agreement about what the role of the MLG should be. Some felt that strong central control over the local authorities was necessary, while others felt that local authorities needed a much greater degree of autonomy. Virtually everyone agreed, however, that the degree of centralized control of the local government system in Kenya is unnecessary, and that it prevents local authorities from operating more efficiently.

The PLGOs, who are highly experienced in local authority affairs, currently have no substantial decision-making authority. Although they do review and analyze most local government requests, the PLGOs do not have much power to act on these requests. They must forward most of their recommendations to the MLG in Nairobi for final action. Most local authority officials seem to have a high regard for the PLGOs, and they believe that the PLGOs are much more familiar than the Nairobi-based officers with conditions in the field. In their current virtually powerless form, however, PLGOs are also seen from a local authority perspective as being little more than an extra layer of delays in the process of securing approval for requests submitted to the MLG.

Internal MLG Problems: Staffing and Procedures

There are a number of serious problems with MLG staffing and the procedures used by MLG officers in performing their assigned duties. These problems may result in arbitrary and delayed action being taken on both routine and extraordinary requests made by local authorities to the MLG.

MLG Organization and Staffing

The organizational structure of the MLG is a frequent target of criticism from local authority officials and PLGOs. Officers from 18 of 26 local authorities have argued that there is insufficient and unclear delegation of responsibility in the central office of the MLG in Nairobi. The officers contend that they often do not know whom to see about particular problems when they arise, because there is no clear designation of responsibilities, at least as far as the local officers know. Local authority officials visiting Nairobi may be sent from one MLG officer to another in an attempt to deal with their problems, and nothing gets resolved or even heard by the right person. There is also the issue of junior- and middle-level MLG officials not having the authority to make many decisions. Thus, there is a strong tendency for local officers to contact very senior level MLG officials directly, even for small requests and problems that arise in the day-to-day running of local authorities. Most of the PLGOs and several MLG officials confirm the existence of these organizational and procedural problems, although they note that many local authority officers prefer to see high-ranking MLG officials for political reasons anyway.

One of the problems most frequently cited by local authority officials is that some of the MLG officials who make decisions about local authorities are recent college graduates who have no practical experience in local authority finance and administration. In spite of this, it is alleged that they sometimes overrule the decisions of the PLGOs, who are senior officials and do have substantial local authority experience. Sometimes this is done without satisfactory explanation. This allegation was supported by all of the PLGOs and several officials from the MLG's central office.

The MLG is greatly understaffed and unable to handle the volume of work for which it is responsible. The number of local authorities and the size and problems of existing ones have grown significantly over the years, while the MLG staff has grown comparatively slowly. This means that there are often long delays in processing even the most routine requests from local authorities.

Excessive Delays in Processing Local Authority Requests

The most consistent and strongest complaint about the Ministry is the excessive delays encountered by the local authorities in obtaining MLG approval of requests. Officials from all 26 local authorities studied cited this as a widespread problem that affects even some of the more efficient councils. It is not at all uncommon for approvals of schedules of fees and charges to be received after the date on which they were supposed to go into effect. This creates problems for the local authorities if they have already started collecting the charges--they may have to make refunds or collect additional revenue depending on whether the old or new charges were being collected and what changes were made by the MLG. This problem is exacerbated by the fact that, as discussed in the previous chapter, the MLG has no standard guidelines for evaluating fee and charge levels.

It is also not unusual for a local authority to receive MLG approval of its annual budget estimates near or even after the end of the year under consideration. Technically, it is not legal for the local authorities to spend or raise revenue without ministerial approval, but some local authorities operate in this way on a year-to-year basis, making the process of submitting estimates virtually meaningless.

The local authorities also share a significant part of the blame for the delays involved in estimate approvals. Although there are clearly major bottlenecks in the MLG, some local authorities submit their estimates to the provincial offices much too late for them to be approved on time. The PLGOs, who are the liaisons between the local authorities and the MLG, agree unanimously that the blame for delays in approving the estimates must be placed on both the local authorities and the MLG.

Long delays in the approval of by-laws are not uncommon, largely because the MLG does not have a legal section and must process these requests through the Office of the Attorney General. In a few cases, several years have passed without the necessary approval forthcoming. This can make some types of revenue collection very difficult or impossible for the affected local authorities.

Another area in which excessive delays are a problem is the MLG approval of employment requests. Local authorities are not permitted to hire new employees of a certain grade and above, even to replace those slots left open by death or retirement, without MLG approval. Such approvals sometimes take long periods of time, so that vacancies or "acting" appointments may drag on for a year or more. In some cases, it takes a year or more for a vacant position even to be advertised.

MLG Communication of Policies to Local Authorities

There were a number of complaints from local authority officials and PLGOs about the timeliness and presentation of official MLG circulars.[1] Local officials indicated that the assignments outlined in important circulars are sometimes unclear, and that responses to clarification requests are often very slow in coming from the MLG.

Perhaps even more important than unclear circulars is the fact that they are sometimes sent out so late that officials have difficulty implementing the orders by the required date. Several officials even complained of receiving circulars postmarked from Nairobi significantly later than the date when the order was supposed to go into effect.

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[1] Circulars are official communications from a Government of Kenya Ministry outlining official procedures and guidelines. For example, local authorities receive circulars from the Ministry of Local Government detailing how to prepare their budgets estimates or the procedures for hiring new employees.

Finally, some local authority circulars on important guidelines and procedures were issued ten or more years ago and have not been updated to reflect changing conditions. Several local authority officers and PLGOs have argued that a number of standing local authority circulars are irrelevant and unrealistic because they have not been reviewed to determine where revisions are required.

Effect of MLG on Revenue Position of Local Authorities

The most important consequence of inadequate staffing and deficient procedures and guidelines in the MLG is the frequently arbitrary pattern of use of local authority revenue sources, which was documented in the previous chapter. Although all local authorities seem to be allowed to collect license fees, market fees, and a few other fairly standard sources of revenue, the disparity in permission granted to use some sources is extensive. Some local authorities are wealthy merely because they have been granted permission to levy cess on coffee or some other cash crop. Some other coffee-growing districts, however, have not been permitted historically to charge cess. As a result, they are much poorer than their counterparts, or they must tax themselves much more heavily from other sources. The same situation exists with cess on other crops and land rates as well: Some local authorities have been permitted to raise income from these sources and others have not. Although there may be theoretical guidelines, access to certain other sources of revenue seems just as arbitrary. Some councils, for example, receive significant forest fee revenue from the central government for protected forest lands within their jurisdiction, while others do not. These inconsistencies in granting revenue sources to local authorities are clearly one of the main reasons for the interjurisdictional spending disparities documented in Chapters 4 and 5.

In addition to the problem of inconsistency in allowable revenue sources across local authorities, there is also the issue of greatly different rates on many revenue sources across local authorities, which was detailed in Chapter 5. Of course, local authorities are different and are subject to local political pressures, so there will always be some degree of rate disparity. But sometimes similar local authorities may have very different rates, even though the ones with lower rates may have applied to the Ministry for rate increases. Although there are good reasons to remain flexible on this issue and avoid full standardization, the MLG has developed no standards and criteria for making decisions about local tax rates and charges, as discussed in detail earlier. Differences in rates rarely seem to be justifiable, based on differences in type of council, differences in area wealth, or differences in local preferences as expressed through informed local government council decisions.

Overall MLG Policy and Control

Perhaps the single greatest inefficiency with MLG policy is its underlying tendency to treat all local authorities as if they were the same. This might not be fully true in practice--there are some signs that the Ministry may be less likely to modify the estimates of financially capable local authorities. In terms of required submissions and procedures, however, the same degree of control and monitoring basically takes place for all local authorities. This prevents the Ministry from using its limited resources to concentrate on the local authorities that are most in need of attention. Although a case can be made for the MLG to retain its general guardian/watchdog function over all local authorities, governing all local authorities as if they were equally insolvent and/or corrupt and/or poorly managed is clearly counterproductive.

The inefficiency of MLG operations is highlighted by the fact that the MLG seems to have very little real control over what is going on in any of the local authorities. There is a fairly widespread consensus among local authority officers, PLGOs, and even some MLG officers that technical assistance and monitoring on financial matters by MLG is lacking. Despite the facade of strict control, i.e., the requirement that the Ministry approve almost everything of any consequence and some decisions of little consequence, such approvals often come so late as to be relatively meaningless. By conducting the required review processes and eventually issuing approvals, the MLG may be fulfilling the letter of the law, but certainly not its spirit and intent. Effective control and monitoring in other important areas is lacking as well. Some local authorities have not produced audited final financial accounts in 10 or 15 years, if ever. Other local authorities have never, or rarely, made payments on their long-outstanding debt. Treasurers in several of these councils have indicated that in the five, ten, or more years that they have been in office, no officials from MLG have ever even asked why they have not produced final accounts or paid their debts, much less tried to do something about it.

In short, the local authorities in Kenya are subject to a great deal of control, which is arbitrarily, inconsistently, and inadequately administered. Although this control can have serious effects on local authority performance, it is, in some important respects, extremely perfunctory. If the MLG actually knew what was going on in the local authorities and had control over the situation, they would be more likely to be able to do something about the genuinely inefficient and corrupt local authorities. As things currently stand, some of the local authorities with the greatest problems seem to be among the most neglected.

The above criticisms are levied with the understanding that MLG has resource and staffing problems of its own that need to be solved by the Government of Kenya if the MLG is ever to be able to operate at its full potential in its role of supporting local authorities. Given the political realities of Kenya, it is clear that the MLG will continue to have a strong regulatory role to play in the managing of local authorities, although the nature and degree of that control may be open to debate. It is also clear, however, that at this point in time there is a great deal of room for improving the equity and efficiency with which MLG discharges its responsibilities. Although there may be much room for improvement in the local authorities as well, the MLG clearly creates and exacerbates some of the current problems of local authorities through inconsistent and arbitrary decisions on local revenue sources, excessive delays in approving local authority requests, and negligence in monitoring and helping to rectify some of the truly serious problems of local authorities, such as corruption and insolvency.

It is important to note that the MLG has been intensifying its efforts recently to deal with many of the institutional and procedural problems discussed above. Many of the required changes are difficult and slow to implement, but MLG officials are clearly beginning to move in the direction of instituting important reforms in MLG procedures and policies, as will be discussed in Chapter 7. It is far from clear, however, that the MLG will be given the support they need from the central government.

Intergovernmental Grants

There is very little to say about central government grants to local authorities in Kenya because, despite the urgent need for grant programs to deal with interjurisdictional fiscal disparities and the lack of basic local services in some areas, there are very few of them. As noted in Chapter 4, there used to be a substantial system of grants to the local authorities during the colonial period and in the 1960s after independence was established. For example, between 1964 and 1969, grants to all county councils ranged from 21.3 to 30.1 percent of their total expenditures [Colebatch (1974), p. 69]. As explained in Chapter 4, grant programs to local authorities have been gradually eliminated since 1970, and now only two grant programs of any importance exist.

The most important grant program in Kenya is the Ministry of Education's grants for teachers salaries, which go to the large municipalities that have retained responsibility for education. In fiscal year 1985, 70 percent of the 14.3 million Kenyan pounds in central government grants to local authorities was for teachers salaries. Education is one of the main expenditure functions of these municipal councils, and teachers salaries are the largest expense; therefore, this grant can be fairly important. In the three large municipal councils examined for this study, grants for teachers salaries accounted for an average of 23.6 percent of total council revenue. However, aggregate central government grants for all purposes accounted for only 7.3 percent of aggregate municipal council revenues in 1985.[2]

The other grant program is made from a small annual allocation to the Minister for Local Government to assist "needy" councils. There are no specific criteria for defining "needy," so that the money is distributed according to the Minister's judgement. The grants are usually small, somewhere between 2,000 and 15,000 Kenyan pounds, and they almost invariably go to county councils, often in the semi-arid areas. Among the 13 county councils studied for this report, 6 received needy council grants, which accounted for an average of 8.9 percent of their total revenue. Other types of councils are not usually awarded these grants, although at least one town council has received grants in recent years because of extraordinary circumstances. Grants to needy councils represented only 3.5 percent of central government grants to local authorities in 1985.[3]

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[2] This figure was calculated from data in the Economic Survey, 1987 (Nairobi: Central Bureau of Statistics, Ministry of Planning and National Development, 1987), Chapter 6.

[3] The 3.5 percent figure for grants to needy councils and the 70 percent figure for grants for teachers salaries cited in the previous paragraph do not add up to 100 percent of total central government grants to local authorities for fiscal year 1985. This is because 1985 was the last year of

Furthermore central government grants accounted for only 1.5 percent of total revenue in all non-municipal councils in the same year.[4]

Local Authority Capital Financing

Local authorities in Kenya are permitted to borrow on the open market, but few can afford commercial interest rates, and most would be considered poor credit risks. In recent years, a few booming communities have successfully applied for loans from private institutions, but this is a very rare occurrence.

The vast majority of financing for local authority capital investments comes from a central government authority overseen by the Ministry of Local Government. As noted in Chapter 4, the Local Government Loans Authority (LGLA) has been poorly managed and has a reputation for allocating funds on arbitrary or political grounds. It has also been extremely inefficient at recovering the loans it has made, and it has been unable to provide the volume of capital required for basic local authority infrastructure. Nevertheless, it is, and will for the foreseeable future remain, the main source of investment finance for the local

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the phasing out of various other grant programs, which was described in Chapter 4.

[4] This figure was calculated from data in the Economic Survey, 1987 (Nairobi: Central Bureau of Statistics, Ministry of Planning and National Development, 1987), Chapter 6.

authorities. Because of its importance, the Government has made it a priority to reorganize and revitalize the institution, an issue that will be discussed in the next chapter.

Relationship Between Local Authorities, Other Central Government Ministries, and Provincial Administration

Although the Ministry of Local Government is the primary link between the central government and the local authority, there are working relationships between the local authorities and other operating ministries. The Ministry of Works, Housing, and Physical Planning (MWHPP) is in charge of physical development plans and infrastructure development. The Ministry of Lands and Settlement (MLS) deals with land issues and does the surveying and valuation for all local authorities except for some portion of a few of the largest cities, such as Nairobi, Mombasa, and Kisumu. Other ministries work with the local authorities on specific projects. A local authority wishing to be a water provider, for example, must obtain permission from and work with the Ministry of Water Development (MWD). Similarly, local authorities wishing to provide veterinary facilities or a dispensary must work closely with the Ministry of Livestock Development (MLD) or the Ministry of Health (MOH). In other cases, specific services are provided on a one-time basis by a central government office. The Attorney General's Chambers, for example, must prepare and approve by-laws that give the local authorities power to undertake certain of their functions, such as raising revenue from a specific source.

Coordination between local authorities and these ministries is often plagued by problems of bureaucratic delay, inadequate technical and financial assistance, and lack of staff at the central ministries. Many specific projects suffer long delays or never get off the ground because of these problems. Sometimes a ministry is supposed to provide an ongoing service that the local authorities rely on, but the Ministry is unable to keep up with its commitments. Local authority land, for example, is supposed to be revalued at least every five years, and supplementary valuation rolls are supposed to be prepared every year by the Ministry of Lands and Settlement. The MLS, however, is literally years behind schedule, and some local authorities are just having their 1983 or 1984 revaluations conducted. The Attorney General's Chambers sometimes take years to approve local authority by-laws.

These types of delays can cause serious problems for local authorities. Needed services are not provided in a timely fashion, and the revenue base can also be eroded. If the Ministry of Works, Housing and Physical Planning takes more than a year to provide designs for a housing scheme or the Ministry of Water Development delays in organizing water provision, residents of local authorities are denied basic services that they need and are willing to pay for. If the Ministry of Lands and Settlement does not do revaluations on a regular basis or the Attorney General does not approve by-laws enabling local authorities to collect a particular fee or tax, the local authorities can be left in a serious financial situation.

Local authorities also have close relationships with the provincial administration, which includes the district administration and all decentralized offices of the Office of the President. An important policy greatly affecting the relationship between provincial administration and local authorities in Kenya is the District Focus for Rural Development strategy, which became operational in July 1983. This deconcentration policy involves shifting the responsibilities for planning and implementing rural development from the Nairobi headquarters of the ministries to the district level. The District Development Committees (DDCs) are the district level bodies with responsibility for implementing District Focus. Basically, District Focus is designed to generate greater local input into district development projects. Although the ministries retain responsibility for general policies and the planning of multidistrict and national programmes, districts have been delegated responsibility for the operational aspects of district-specific rural development projects. Districts are also responsible for the implementation of district-specific subcomponents of national or multidistrict activities. DDC responsibility for planning and coordination of development activities covers not only projects sponsored by the ministries, but also projects supported by Harambee, local authorities, nongovernmental organizations, and foreign donors.

Local authorities are required to submit their planned development projects to the DDCs before they are forwarded to the Ministry of Local Government for approval and help in identifying sources of funding. Projects being jointly implemented by a local authority and a ministry must also go through this review process. The purpose of DDC approval is to ensure coordination of local authority projects with other development activities in the district.

Although there seems to be a great deal of support for the concept of District Focus, there also seems to be much confusion and dissatisfaction among local authority officials with the way in which District Focus is currently being implemented, at least with respect to the relationship between the DDC and local authorities. Some local authority officers regard the DDC as a rubber-stamp organization, as nothing more than another level of bureaucracy through which they must channel their project plans, and there is evidence in some districts to back up these allegations. In a few cases, there is a lot of friction between local authorities and the DDC--there are examples of DDCs holding up local authority capital projects for as long as several years, even in cases in which the local authority had clearly demonstrated its financial capacity to undertake the project as well as the need for it. In these cases there is apparently a great deal of political infighting that slows down the review process.

There is a strong feeling among local authority officials that local authorities are inadequately represented on the DDCs. Officials from half of the local authorities under study have cited this as a major concern. The only two official members of the DDC from local authorities among the fifty or more total members are the Clerk to Council, an appointed officer who is the chief administrator, and the Chairman of the Council, an elected official. There are also Members of Parliament and District Officers on the committee, but it is dominated by technocrats from the central government ministries, many of whom are not from the local area but have been assigned to the district from Nairobi. Thus, there is a feeling that the organization that is supposed to be soliciting input from local people is not really the grassroots organization it is so often claimed to be by national politicians.[5] Yet, this organization has a great deal of control over most of the development projects

[5] It is clear from a careful reading of the District Focus for Rural Development guidelines that the strategy is one of deconcentration rather than devolution. It is normally discussed by politicians and the press, however, as if it were genuine grassroots decentralization.

undertaken locally.

It should be noted that divisional DDCs, which function in specific areas of the districts, have much more local representation that the DDCs, but in many places they are not very powerful and in some areas may not be active at all.[6] If the decentralized DDCs were more effective, it might be argued that the largely technocratic and nonlocal composition of the DDC is a good thing. The decentralized groups would provide the local input, while the main DDC would add an element of technical expertise and objectivity to the system, possibly minimizing the number of decisions based purely on local/tribal politics. This is the direction in which the process is supposed to be moving, but whether or not it will be successful remains to be seen.

Perhaps the strongest complaint registered by local authority officers regarding District Development Committees is that they do not provide any funding to local authorities or help them to identify potential sources of funding. Although it may be argued that the DDC is not required to fund local authorities, it is legally possible for the DDC to identify and fund rural development projects to be constructed and operated by a county council. It has been argued that such projects might improve the relationship

[6] The divisions, locations, and sublocations of districts are permitted to organize development committees to channel information on needs and problems to the DDCs, but few places have yet organized such an extensive network of local input.

between rural local authorities and the DDCs, and serve to provide additional revenue-generating projects for some local authorities.

The DDCs do a poor job of initiating coordination among local authorities for mutually beneficial projects. As noted earlier, not a single case of such inter-council cooperation was discovered in any of the districts visited for this study. This type of coordination is supposed to be the responsibility of the DDCs. They have the power to require coordination, which has the potential to introduce greater efficiency and reduce certain inequities in the provision of local authority services.

In summary, the concept of District Focus is sound and desirable and the idea of a stronger and more cooperative relationship among local authorities, district officers of the central government ministries and decentralized representatives of the Office of the President is a good one. In a strong centralized state such as Kenya, the local authorities will be able to operate more effectively if they have the cooperation and support of the most powerful elements of the central government. The current implementation of the new policy, however, has not yet realized much of its valuable potential.

Local Institutional Capacity and Procedures

Having examined intergovernmental institutional issues relevant to local authorities in Kenya, it is appropriate to turn to a discussion of problems with local institutional capacity and procedures. It is somewhat misleading to isolate these problems as "local" because central government actions and policies, or lack thereof, can greatly affect local institutional organization and performance. Nevertheless, these problems are largely local in their impact, and it is useful to make this distinction for purposes of the analysis.

A variety of local institutional problems currently exist in Kenya, many of which have already been mentioned in this evaluation. These problems, which have a tremendous impact on the fiscal role and financial viability of local authorities, will be explored in greater detail in this section. Particular attention is paid to general administration and management problems, the most important of which relate to local authority revenue generation. There is also some discussion of how conflict between appointed officers and elected officials sometimes leads to poor fiscal decisions in local authorities.

General Management and Administration Problems

The local authority accounting procedures inherited by Kenya from the British seem to be cumbersome and difficult for most councils to use effectively. The detailed and complicated system of final accounts that are supposed to be prepared at the end of each financial year are a particular problem. Although some local authorities are reasonably up to date in their final accounts, most are at least a few years behind, some are 10 or 20 years behind, and some have never produced them.

In general, the system of record-keeping in local authorities is inadequate. Poor and inaccurate records kept on council financial transactions lead to poor revenue and expenditure management and control, and make it very difficult to plan for the future and prepare forward budgets. Data on specific revenue/activity at particular revenue collection sites, for example, would help the local authority officers to monitor and project their revenue trends for that source of revenue more accurately. This type of detailed data is very rarely kept.

In some local authorities, the process of preparing budget estimates is not a very meaningful exercise. These estimates often include revenues that the council knows it will not be able to collect, and the revenue projections, in some cases, seem arbitrary. Things are not much better on the expenditure side. Because of poor expenditure management and control, the budgeted figures for some categories of spending are meaningless, as they are often not used as expenditure ceilings. After the budgeted amount has been spent, some councils just keep on spending.

Cash-flow management is a serious problem in many local authorities because a great deal of council revenues often come in during only a few months, while expenditures are made on an ongoing basis. Some local authorities seem to make little effort to deal with this problem. They spend all of their money when it comes in and then have none to cover even basic expenditures, such as salaries, later in the year. It should be emphasized that such extreme behavior happens largely in very poor councils, but there is room for improved cash-flow management in other local authorities as well.

There is a serious problem with a lack of incentives for local authority employees, a problem that is shared with the Kenyan Civil Service. The pay scale is very low compared with the private sector, and there is no clear system for raises and promotions. In addition, there are few benefits or opportunities for bonuses. The result is that the local authorities to a significant extent employ those who cannot find private sector employment. These employees have little incentive to work hard, and there is substantial inertia, low productivity, and some degree of corruption in many local authorities.

A significant number of local officers lack the training, experience, and skills required to discharge their responsibilities properly. MLG and USAID have instituted a training program for local authority officers, which will help deal with this problem, and the Kenya Institute of Administration in Nairobi and the Government Training

Institute at Mombasa offer a wide variety of courses for local authority employees. Thus, the government is well aware of the problem and is expanding its efforts to alleviate it. Some of the training programs, however, are superficial and poorly conceived. In any case, no training program can be expected to have a major impact unless some of the major institutional constraints being discussed in this chapter are relaxed.

There is also a problem of dishonesty and misuse of council funds by some local authority officers. In most local authorities visited for this study, proper internal auditing and cross-checking of records were greatly lacking. The internal auditor in Kenyan local authorities is directly under the control of the treasurer, the individual who controls the council's money. Interviews conducted with several internal auditors for this study indicate that a number of them are extremely frustrated with what they perceive as improper or excessive spending in certain categories. They may protest to the treasurer or a councillor up to a certain point, but they generally fear for their jobs and do not feel that they have the security to pursue the issue. Again, it is important to emphasize that this is not a problem in all councils, but it is clearly a major issue in some.

Revenue Collection

The most important administrative problem for many local authorities is their inability to collect fully the revenue that is due to them. Some types of revenue are relatively easy to collect because there are simple ways to deal with defaulters. If, for example, a resident does not pay water/sewerage fees or house rents, it is easy to turn off water or evict the tenant as long as there are not political obstacles to doing so. Similarly, if a trader does not pay the annual license fee, he/she can be refused other services or have his/her business closed down. Some revenue sources are not even collected directly by the local authority--certain cesses are collected by central marketing boards and the local authority's only collection effort is depositing the check it receives from the board.

With many types of local taxes, however, it is much more difficult to collect revenue. In some cases, local authorities collect only 25-50% of the revenue they should receive from a particular source. There are five principal reasons for these collection difficulties: (1) lack of collection and enforcement personnel; (2) dishonesty of some revenue collectors; (3) lack of proper enforcement authority; (4) political pressure on local officers to be less aggressive in revenue collection; and, (5) great delinquency on the part of some government agencies and parastatals. Each of these issues will be discussed in turn.

Lack of Enforcement/Collection Personnel

Although some local authorities claim to have enough collection personnel, many are clearly understaffed, a problem that affects almost all sources of revenue. Officials from 15 of 26 local authorities reported that they had an inadequate number of revenue collectors. Market-related activities tend to be a problem, especially in areas without properly fenced markets and stock auction yards. In some cases, very large markets are staffed by as few as two or three revenue collectors. Lack of staff can be a crippling problem in some county councils, where there are sometimes not enough revenue collectors to assign even one to every division.

In such cases, revenue collectors must travel between divisions, making collection more sporadic and difficult to enforce. These traveling revenue collectors are sometimes further hampered by lack of adequate and reliable transportation, a problem mentioned by officials from eight county councils. Some county councils cannot afford to buy new vehicles or to keep their old vehicles in good repair, and petrol becomes a major expense. Monitoring revenue collections in this type of situation is very nearly impossible.

Lack of enforcement personnel is also an issue here. Many local authorities do not have enough staff to send them around regularly to help collect unpaid land rates, unpaid license fees, unpaid house rents, etc. Officials in 21 of the 26 local authorities indicated that they had insufficient enforcement staff. In order to evade local authority fees, matatu and bus drivers may attempt to pick up passengers outside of the bus park, and livestock owners may try to conduct sales outside of the stock auction yard. Without proper enforcement personnel, it is difficult to monitor these activities, and the council may lose significant revenues. It should be noted that some councils get enforcement help from the Kenya Police and the District Commissioner's Office, but the quality and regularity of such assistance varies considerably, and it is not forthcoming at all in some areas.

The collection problems for some taxes have been complicated by certain government policies. Collecting agricultural land rates, for example, used to be less difficult when much of the agricultural land in the former settler areas was in large holdings. Since the government instituted policies of subdividing and redistributing land, the pressure on revenue collection and enforcement personnel has increased many fold. Not only are there more ratepayers to collect from, but they are generally poorer than the previous landholders and less able to pay the land rates. In addition, there is a high incidence of absentee land ownership in some of the areas where subdivision has taken place, further frustrating the revenue collection process.

Dishonesty

Corruption is likely to be a problem of varying degree in most local authorities. Officials in nine local authorities admitted that it was a serious problem in their councils. Because of the lack of enforcement and control in many local authorities, it is relatively easy for revenue collectors to pocket some portion of the cash that they collect each day. There are many ways of doing this. Sometimes the collection officer fails to issue a receipt and is not challenged by the fee payer. In other cases, the fee collector and payer may collude and split the proper fee or some portion of it, sometimes in further collusion with the enforcement officer. It is also possible for revenue collectors to trick illiterate fee payers by giving them a receipt for less than the amount of money they have actually collected, thus allowing the collector to pocket the difference unnoticed.

A problem related to the dishonesty of some revenue collectors is the failure of some local authority officers to take proper investigative and/or disciplinary action against employees suspected of or proven to be cheating. Some local officers will argue that "the employee he replaced was worse" or, "the process of hiring and firing is too difficult and time-consuming", or "he is a brother-in-law of one of the councillors." Some of these officers may also be misusing public funds, or they may be fearful of losing their jobs or undermining their working relationships with their councils.

Lack of Enforcement Authority

Lack of proper enforcement authority was mentioned by officials in 17 of 26 local authorities as being a major problem, even in those councils that are adequately staffed. In some cases, local authorities do not have proper by-laws for some sources of revenue. This is a problem especially in places where residents are aware of the lack of by-laws and refuse to pay the tax in question. The lack of by-laws is sometimes due to negligence on the part of the local authority, but it is often due to long delays in approval of submitted by-laws by the Ministry of Local Government and the Attorney General's Chambers, as discussed earlier.

Even in places in which proper by-laws are in place, local officers lack strong legal authority to collect some sources of revenue and the legal machinery for collection is very complex and cumbersome. The primary example of this is land rates, which is one of the most important sources of local authority revenue in Kenya, both in urban areas and rural areas where it is permitted. There are certain things local authorities can do to enforce land rate collection, such as require tenants of a plot in arrears to pay rent to the council instead of the landlords. However, in addition to being politically difficult to implement in some places, the power of force is not really there. The local authority itself cannot fine or take delinquent taxpayers to jail, nor does it retain the power of sale for serious defaulters. It must operate through the national legal system, which has several disadvantages. First, there are long delays in the legal system, and recovery of revenue usually takes a great deal of time. Second, most local authorities do not have their own advocate and must therefore hire one to represent them. Legal costs are often so high that they are not covered by the revenue that would be collected in a successful case. There are also several instances in which lawyers have kept all of the money recovered from those prosecuted by the local authorities. In such cases, the local authority is faced with the undesirable choice of instituting further costly legal proceedings or simply dropping the matter to minimize their losses.

Local Political Pressure

Political pressure is another major revenue collection problem faced by some local authorities. Officials in eight local authorities cited it as a major obstacle to better collection. This problem stems from the fact that taxes are universally unpopular and elected councillors who wish to be re-elected have a great desire to be popular.

As a result, there are sometimes cases when councillors intervene in an attempt to prevent water from being turned off for default on the water/sewerage bill, to prevent tenants from being evicted for not paying rent on council-owned housing, etc. Councillors are often reluctant to raise taxes and charges, even if they have not been raised in some time and the council is consistently running a deficit. This is true not only because of the popularity issue, but also because councillors are sometimes major landowners or prominent businessmen in the local area, and they see the higher taxes as having a direct negative effect on them.

Delinquency of Government of Kenya (GOK) & Parastatals

Another important problem faced to some extent by almost every local authority examined in this study is the delinquency of government agencies and parastatals in submitting the taxes, charges, and payments they owe to local authorities. Officials in 16 local authorities cited this as one of their most serious revenue problems. In some cases, local authorities claim to be owed millions of Kenyan shillings by these delinquent groups. The problem seems to persist for several reasons. First, the claims of local authorities are sometimes disputed by the alleged defaulter and the disputes have not been properly resolved, even after many years. The most frequent case of this is Kenya Railways, but it is a problem with others as well. Second, GOK ministries rarely budget enough money for their district offices to be able to pay for such local authority services as sewerage and water and for payments in lieu of taxes. Thus, revenues from district offices are sometimes very late or never arrive. Finally, local authority officers lack any real authority to enforce the collection of such revenue. The local authorities cannot easily turn off the water supplies of such services as schools, prisons, and hospitals, and they cannot force central government ministries or other local authorities to pay for such services. In some instances in which a local authority has tried to take a debtor local authority or parastatal to court, the MLG has intervened on the grounds that it is not good to involve a sister local authority or important parastatal in litigation. In essence, this revenue has become uncollectible from a practical point of view.

Local Government Internal Structure: Relationship Between Elected Councillors and Appointed Officers

There are always some natural tensions between elected and appointed officials in any system of government, and the local authority system in Kenya is no exception. These tensions need to be monitored so that neither group is able to use its position of responsibility and authority improperly. As noted earlier in the discussion of revenue collection, local politics sometimes seriously interfere with the fiscal operations of local government.

In some local authorities, there is local political pressure for spending not in the public's best interest, and there may also be cases of improper use of council funds by councillors and/or officers. The first problem often takes the form of projects that are undertaken to benefit a small group of people or to help assure that re-election votes will be forthcoming. Such projects may not be inherently bad, but the money might have been spent better.

The problem of improper use of council funds is a difficult one to deal with. It is clear, however, that lack of proper internal auditing in many councils is a tremendous contributing factor to this problem. The generally poor expenditure control in most local authorities and the lack of independence of internal auditors, both of which were discussed earlier, are major factors that inhibit more accurate and honest monitoring of local authority expenditure.

A problem often cited by local authority officers regarding their relationship with elected councillors is the lack of training of some councillors, especially in more rural areas. Although these councillors have been duly elected and may truly represent their constituency, some may be uneducated or even illiterate, and they may not fully understand the way the local government system works. Although such councillors are often very open to the advice of their appointed officers, some can create problems because their idea of how things are done may be unrealistic. A councillor who knows absolutely nothing about finance, for example, may be elected Chairman of the Finance Committee of his council, and he may try to tell the treasurer how to run the finances of the council. Although this problem is not very widespread, it does cause serious problems in the affected councils.

In some local authorities, local officers seem to create some of their own problems with the council by forming alliances with groups of councillors with whom they tend to agree. This type of behavior may cause resentment on the part of other councillors, who then may try to make life more difficult for the local official. The end result may be that some taxes do not get collected and some services do not get provided. Local officials and elected councillors have a job to do, which requires that they maintain a professional relationship. Forming alliances may undermine the overall goodwill and stability of this relationship and should be avoided as much as possible.

Summary of Public Finance and Institutional Issues

Chapters 5 and 6 have discussed the major public finance and institutional issues relevant to an evaluation of the fiscal role of local government in Kenya. As discussed in Chapter 5, the pattern of services provided by the central government and local authorities in Kenya is basically rational on economic grounds. There are a few services for which responsibility is not clearly or rationally assigned or self-assigned, but the basic division of responsibilities is normally reasonable. Local governments in Kenya also have access to a wide variety of revenue sources, at least legally. In reality, however, there are problems with both service provision and revenue generation.

The most significant problem facing a majority of local authorities is a lack of access to sufficiently productive, reliable, and collectible financial resources. Many sources of local authority revenue are relatively static, subject to extreme fluctuations in response to changes in the local economy, or subject to arbitrary control by the central government. In many areas, local taxes are inequitable and inefficient, although a variety of offsetting factors probably prevent serious spatial efficiency effects from occurring.

The correspondence between expenditures and revenue sources is, in general, fairly reasonable for municipal councils, but often inadequate for councils in rural areas. Across all types of councils, there are unsatisfactory guidelines and procedures for setting tax rates and user fees. The lack of a rational basis for determining rates and charges often means that they are set at a level inadequate to cover the costs of service provision. There is also a lack of central government grant programs for local authorities even though they are clearly needed.

Major intergovernmental and institutional factors have the most dramatic impact on the ability of local authorities to perform their fiscal functions. Most importantly, restrictive, cumbersome, and inefficient policies and procedures in the Ministry of Local Government can cause or further complicate some local authority problems. The inconsistent and arbitrary assignment of revenue authority to local authorities is particularly a problem. It leads to enormous fiscal disparities and differences in spending levels across local authorities. Less serious, but significant, are the poorly defined and inconsistently implemented relationships that exist between local authorities and certain central government institutions, including the District Development Committees and some government ministries.

Local institutional deficiencies are significant in most Kenyan local authorities. Poor financial management, lack of employee incentives, and inadequate training, some of which could be improved by central government intervention, exacerbate many local authority revenue and expenditure difficulties. Probably the most serious local institutional constraint is the revenue collection problems that exist in a majority of local authorities. Some of these collection problems are beyond the control of local authority officers. Dishonesty, lack of collection and enforcement staff, lack of compliance by government agencies and parastatals, lack of legal enforcement authority, and political pressure are all significant problems in many areas.

The result of these problems and constraints is that a majority of local authorities in Kenya are struggling to make ends meet, and some have been for many years. Many consistently run deficits, and a significant number are heavily in debt, which they are unable to repay. Access to capital is inadequate, investment in infrastructure is generally low and maintenance is poor, and many services are of low quality and are provided at insufficient levels.

The various types of local authorities suffer in different ways. Older, more established municipal councils are plagued by an inability to provide major services adequately and to maintain or replace deteriorating infrastructure. Newer municipal and town councils are faced with finding a way to provide basic infrastructure without the massive infusion of central government aid that helped to build the infrastructure in the older urban areas. County councils are in a particularly precarious position: many of them, especially in the more rural areas, are able to provide few tangible services, have few sources of revenue, and maintain relatively large employee rolls.

The bottom line is that many local authorities in Kenya are in very poor shape. If they continue to exist in their current state, some will be able to do little more than inadequately provide a few services and continue accumulating debt. Thus, the Government of Kenya is faced with the difficult problem of deciding what it wants to do about local authorities.

If local authorities in Kenya are going to be able to exist over the long term in any fiscally meaningful way, it eventually will be impossible to avoid implementing major reforms in the local government system, particularly with respect to institutional relationships and procedures. Some required reforms can most likely be instituted fairly easily, while others are more politically controversial and difficult to implement. Although the problem of limited human and financial resources greatly affects the fiscal role and performance of local government, political constraints have clearly been the major obstacle to more effective local government in Kenya. Meaningful reform cannot take place unless there exists the political will required to strengthen local authorities and accord them a more substantive role in the country's development process. The next chapter will look at a variety of possible reforms of the local authority system in Kenya.

CHAPTER 7

STRENGTHENING THE FISCAL ROLE OF LOCAL GOVERNMENT IN KENYA: OPTIONS FOR REFORM

The previous chapters were critical of many aspects of the fiscal role and operation of local government in Kenya. The failures of local government negatively affect the efficiency of resource use and the quality of life. Inefficient and ineffective local authorities have an impact not only on the provision of local services, but also on the progress achieved in implementing national development strategies. As discussed in Chapter 1, local government is only one component of an integrated and coordinated system of national and local institutions that should be working together in pursuit of common goals. To the extent that local authorities are unable to meet their share of the responsibilities, the attainment of national development goals is undermined.

The task of this chapter is to discuss potential reforms of the various dimensions of the local government system on which the evaluation in Chapters 5 and 6 was based. These include service provision, revenue generation, and institutional issues. These distinctions are somewhat artificial because all of these areas and issues are highly interrelated. Some reforms, however, are more related to one particular area than the others. The interrelationships across areas will be explicitly recognized and discussed, and the relative importance of various reforms will be noted. Some of these reforms could begin almost immediately if the Government of Kenya is willing to take action. Other reforms will take a longer time to institute, because more careful thought and research are required or because there are particularly difficult implementation problems resulting from major political, technical, financial, or legal constraints. With some of these reforms, there are very clear steps that will need to be taken in order to correct or alleviate a particular problem. In other cases, there are a variety of options that could be considered to improve the situation.

National Political Considerations

As demonstrated in Chapter 4, local authorities in Kenya are responsible for only a small percentage of public spending. Nevertheless, they do provide many basic public services to the people of Kenya; therefore, they have an important role to play. They also have the potential to make a much greater impact on the quality of people's lives than they currently do. Unfortunately, a variety of political, economic, and institutional constraints prevent many local authorities from meeting their potential. Most of these constraints are within the power of the central government to deal with, at least to some extent. A carefully planned program of public policies and interventions could tremendously strengthen local authorities and enable them to fulfill their responsibilities more effectively than at present. Some of these policies could have an almost immediate effect, while others would be slowly felt over a period of years.

It is far from clear that the Government of Kenya has any genuine interest in strengthening local authorities. It was well documented in Chapter 4 that the central government seems to have done everything in its power to take responsibilities away from the local authorities over the years since independence. It is not at all an exaggeration to state that the central government is largely to blame for the poor state of Kenyan local government today. In recent years, particularly in the wake of the August 1982 coup attempt, the government has continued to implement policies designed to consolidate power at the center in the hands of the ruling party, and it has greatly neglected local authorities.

Despite this historical tendency towards strong centralization, there is reason for some optimism that local government in Kenya will be strengthened. Many of the issues discussed in Chapter 1 clearly apply to Kenya. The country's population and service demands are rapidly growing at the same time that ministerial budgets are being cut, pointing to the possibility of greater reliance on local authorities. In addition, it is being increasingly recognized by central government officials that local authorities have an important role to play in implementing national development policies, as was discussed in Chapter 1. In the case of Kenya, the government must face the fact that its rural-urban balance strategy, as discussed in Chapter 3 and Appendix IV, crucially depends on the ability of local authorities to function effectively. In the years since independence, the government has seen many decentralized development projects collapse because there was not adequate administrative, implementation, and recurrent financial capacity available at the local level. National politicians publicly praise Sessional Paper No. 1 of 1986 and the rural-urban balance strategy as a salvation to Kenya's worsening employment and population problems, but no concrete steps have yet been taken to strengthen local government. What many national leaders may not realize is that they are destined to experience a major development policy failure if they do not do something about the problems of local government.

The reality of the situation is that, even if local authorities are substantially strengthened, they will not present any threat to the powerful control over the country exerted by the central government. Local authorities are creations of the central government and can be dissolved at any time by the Minister for Local Government. The only negative effect that central government officials are likely to experience from strengthening local authorities is that some individual Members of Parliament may end up facing strong election challenges from local authority councillors whose councils have been successful in improving service provision to the people in their areas. Some may argue that strengthening local government means strengthening tribalism, but this is little more than an overused excuse for inaction. The major impact of effective local authorities will be the provision of better local services to Kenyan citizens.

During the next few years, the will of the Kenyan Government to revitalize local authorities will be seriously tested. The central government's intention to strengthen local government has been highlighted in policy documents, speeches, and the press. A lot of promises have been made, and both the Ministry of Local Government and the Ministry of Planning and National Development are busy preparing proposals for strengthening local authorities, particularly in the areas of revenue generation and increasing the size and quality of staff. Some of the reforms the Government of Kenya may wish to consider as it reviews the future of local authorities are outlined in the following sections.

Service Provision Reforms

As discussed in Chapter 5, the pattern of service provision that has emerged among levels of government in Kenya is fairly good. It is true there are few specific service requirements of most types of local authority, and it would make sense for the central government to issue explicit guidelines about what types of services should generally be undertaken by different types of council. Most local authorities, however, have independently attempted to provide a reasonable package of services. This is particularly true of municipal and town councils, which take responsiblity for many of the same types of urban services traditionally provided in the developed countries. Many of the rural local authorities, however, are weak, and it is possible to make a strong case for expanding the role of county councils.

As noted in Chapter 4, since being relieved of several major responsibilities in 1969, many of the county councils have been functionally marginalized. Some Kenyans, who have begrudgingly supported the existence of local authorities as token agents of grassroots participation, certainly see this as a desirable thing. They would argue that county councils, particularly the fairly inactive ones, should be abolished and their few responsibilities turned over to the central government ministries. This would not be desirable, however, because of varying preferences due to different economic bases, the limited resources of the central government, and the geographical inaccessibility of some areas. Given all of the high-visibility rhetoric about decentralization in Kenya in recent years, the abolition of county councils is very unlikely, even if they remain only as token institutions.

A far more worthwhile effort would be to define a unique and productive role for county councils to augment their current responsibilities. It is clear, for example, that enhancing the role of local authorities, particularly county councils, as marketing and distribution facilitators would give them a useful role to play as well as provide an important service presently lacking in Kenya. Although most county councils currently facilitate marketing through the provision of markets and stock auction yards, many of these facilities are located only in one or a few major trading centers that may be inaccessible to many district residents. Also, there are no good sources of current marketing/price information on a decentralized basis available in Kenya. Collecting and distributing weekly information on the availability and cost of goods in the districts is a good way of helping people to decide where to buy and sell their products. This type of service could have an important impact on private sector development in the area. Development would be enhanced further if county councils could work to improve impassable roads, which presently hinder the distribution of both agricultural inputs and agricultural products grown in their districts. Preliminary results of a study of rural-urban linkages in Kenya, which is still in progress, suggest that poor access roads in the rural areas are the most significant constraint to the timely distribution of agricultural inputs and production.[1] Improvement of trade in particular areas would give a major boost to county council self-sufficiency and ability to provide services to the people, because most county council revenues are based on private-sector trading activity.

Some strong proponents of local authorities would go so far as to suggest that county councils should shoulder the coordination responsibilities currently undertaken by the District Development Committees, which were explained in the previous chapter. In most cases, counties and districts are geographically identical, and it is argued by proponents of decentralization that local authorities are the true representatives of the local people. Whatever the merits of this point of view, it is very unlikely that the functions of the DDCs will be transferred to local authorities. This would represent a strengthening of local government at the expense of the Office of the President that would be unacceptable to many national politicians and other leaders. In any case, it does make more sense for the central government rather than local authorities to take the lead in coordinating development activities undertaken by different levels of government. It is very likely that the DDCs and

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[1] This study, which will continue into mid-1988, is a cooperative effort of the Government of Kenya, the United States Agency for International Development, the Harvard Institute for International Development, and SARSA/Clark University. It is being conducted in the town of Kutus, which is located in Kirinyaga District of Central Province.

the District Focus for Rural Development are here to stay in their present form, at least for the foreseeable future.

As far as specific services are concerned, it was argued earlier that most services that could be considered local in nature are, in fact, provided locally, while those that exhibit economies of scale or externalities are provided centrally. One exception to this pattern is education. It would be reasonable for the central government to allow local authorities greater responsibility for the provision of education. Cultures and needs differ from area to area, and this could be reflected in the curriculum through local input while still maintaining minimum standards for basic common disciplines; however, as noted in Chapter 5, this is not likely to happen. The educational system is a valuable political tool of the central government, and its devolution to local authorities is not politically feasible.

The other two major services that display problems in their pattern of provision are water and veterinary services. Both can be provided locally, but may require central government intervention for equity reasons and because of potential externalities. The problem is not that both of these services are sometimes provided by the central government and sometimes by local authorities. Rather, the issue is that there are no explicit and rational guidelines by which to make the assignment decision. This has resulted in a situation in which some local authorities who could adequately provide these services are being subsidized by the central government. In other cases, local authorities who cannot provide an efficient level of services are receiving no central government assistance. In the case of water, there is an additional point of concern because of the potential for it to provide a good source of surplus revenue to the councils. Guidelines for assigning both water and veterinary services to levels of government need to be developed.

Another issue related to service provision is the widespread inequity in the spatial pattern of service provision within many local authorities. People in some areas of local authorities have good service provision, while people in other areas have few or no services. In some cases, this is reasonable because certain services are only required in certain types of areas. It may be justifiable, for example, to provide street lighting in urban centers, but such services are not required in other areas. Selective provision of some other services may not be justified, and the local authorities should make efforts to provide them more uniformly. That will be unlikely in many local authorities, however, until their financial and managerial capacity is improved.

In summary, inefficient assignment of service functions between the central and local governments is not a major problem. The poor quality of service provision in many councils and the tremendous variation in per capita expenditures across councils largely result from inadequate revenue generation, intergovernmental and institutional problems, and administrative and managerial constraints.

Revenue Generation Reforms

As noted in Chapter 5, the revenue-expenditure linkage is fairly reasonable for municipal councils. Most of the revenue generation problems of municipal councils come from poor collection and administrative problems rather than from lack of access to income commensurate with service responsibilities. This is not true of many county councils, which clearly do not have access to enough income to provide even their few services, much less assume the expanded role outlined earlier. This can only be solved by standardizing revenue sources available to them and/or allowing some alternative sources of revenue.

Revenue generation is the most crippling problem of Kenyan local authorities, even in those areas that may seem to have a good correspondence between revenues and expenditures. Many of the sources of revenue available to local authorities are inelastic or unstable, and some local authorities are very reliant upon one or two main sources. There are many types of income legally open to local authorities in Kenya, but differences in economic base, problems in revenue collection, and administrative decisions by the Ministry of Local Government can effectively close off important options for many local authorities.

There are four major revenue generation policies in Kenya that will need to be implemented by the central government in order to insure that local authorities can effectively play a significant fiscal role. First, authority to use existing sources of income should be extended to all applicable local authorities, unless there are special circumstances that suggest otherwise. Second, standard and rational guidelines for setting tax rates, fees, and user charges must be developed and used by all local authorities. Third, in many areas, it will be necessary to provide access to additional sources of revenue. Finally, steps must be taken to improve revenue collection. The first three policy areas will be examined in this section, and the fourth will be discussed in the section on local institutional reforms.

Extension of Authority to Use Existing Sources of Income

The first step that should be taken towards improving the revenue position of local authorities in Kenya is standardization of the set of revenue sources allowed to local authorities to as great an extent possible. The inconsistency of current policy causes tremendous, but artificial, disparities in fiscal capacity across local authorities. There are four main types of revenue currently allowed to Kenyan local authorities. These are land rates, user fees and charges, business and trade license fees, and production taxes (cesses). All local authorities are allowed to collect business and trade licenses and user charges, but there is no standardization of access to land rates and cesses. If some local authorities are going to be permitted to use a revenue source not allowed to others, there must be some reasonable justification. For some revenue sources, standardization will require research and take time, but for others the process can be undertaken quickly.

Perhaps the most obvious source of revenue not being collected by many local authorities is cess. Officials from 19 of the 26 councils examined in this study cited expansion and standardization of cess as an important step for the Government of Kenya to take in order to improve the revenue position of local authorities. Some local authorities, as noted earlier, have been collecting cess since colonial days, but many have not been allowed to do so. It would seem fair that all local authorities in areas where land rates are not feasible should be allowed to charge a small standardized cess of perhaps one to three percent on whatever is produced within their jurisdiction, whether agricultural or industrial. Local authorities provide basic services to farmers and manufacturers alike, and in many cases get little or no revenue from these producers. The Government's recent announcement of its intention to allow all county councils to charge a fixed percentage cess on a standardized group of agricultural products is a major step in the right direction, but it is not going to do much for poorer urban areas or arid/semi-arid rural areas where livestock trading is the main economic activity.

An alternative to allowing more widespread use of cess would be to abolish all cesses and substantially upgrade the use of land rates. In rural areas, a few county councils do have rates on agricultural land, but most do not rely on this source of revenue to any significant extent. It essentially taxes the same base as cess; therefore, the two should not be used together. The advantage of cess is that it is based upon the value of production, thus a true tax on economic activity. It is possible, however, that such a tax would have some disincentives for production. Land rates may have the problem of being regressive, but they are more stable because they are based on the value of the land and are less likely to decline in low production years.[2] In addition, collecting a fixed rate on land provides an incentive to produce as much as possible, because any surplus over the value of the rates will be kept by the farmers as profit. A problem arises in that land rates are very difficult to collect without proper enforcement authority and adequate collection personnel. In contrast, most cesses, at least those levied on cash crops, are collected by the marketing

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[2] It should be noted that a problem may still exist to the extent that some farmers/landowners do not have cash income sufficient to pay the tax.

board of the crop in question rather than by the local authorities. The issue of cesses versus land rates is an important issue and merits further consideration by the Government of Kenya. Greater standardization of either would deal with many of the efficiency and equity effects of local authority finance discussed in the previous chapter and would provide an enormous boost in the revenue capacity of many councils. Because of the substantial administrative costs and problems associated with land rates, however, cesses are clearly a more reasonable short-term solution to the revenue problems of rural local authorities, despite their potential lack of stability and efficiency loss.

The use of land rates in urban areas is greatly in need of improvement. In addition to the collection problems, lack of enforcement authority, and delays in revaluing land, all of which were discussed in the previous two chapters, there are other problems as well. In some urban areas, only a small percentage of the land is rated, even in the town centers. This means that shopkeepers and other businessmen in the surveyed area pay taxes on their land, while a businessman with a similar operation one block away in an unsurveyed area pays no land rate at all. This practice is obviously highly inequitable and inefficient--both businesses may get the same services, but only one ends up paying for them. Every effort must be made to survey fully all of the central town areas of local authorities.

As noted in Chapter 5, there are substantial lags in the revaluation of land in local authorities. This can greatly reduce the elasticity of land tax revenue. Although local authorities are technically allowed to raise the rate levied on the base during years when no revaluation occurs, many local authorities are unable to take advantage of this option because of strong local political pressures against it. Even if the local authorities do raise their rates, collection is difficult because of the lack of enforcement authority.

Another issue with land rates in urban areas is that they are levied only on the unimproved site value of parcels of land. There is a great deal of debate on the issue of taxing the developed value of land. On the one hand, a tax on improvements is likely to increase revenue yields, and it may improve efficiency to the extent that more developed land makes more intensive use of services financed from land rates. There is also the possibility that a tax on improvements will be more vertically equitable. The use of an improvements base, however, may tend to discourage intensity of land use and to encourage the speculative withholding of land from the market. Research in Kenya has suggested that a limited movement to tax the developed value of land would be productive, at least in a few of the largest municipal councils. However, there would be major administrative problems to overcome, which might be insurmountable in the short-term [Bahl and Mant, (1976)].

The lack of standardization of land rates and cesses, both within and across local authorities in Kenya, has potential equity and efficiency effects. As noted in Chapter 5, the magnitude of the efficiency effects is not likely to be large, but the equity effects can be enormous. These could be alleviated, to a great extent, by having a more generally applied tax on land or economic activity.

Standard Guidelines for Setting Tax Rates, Fees, and Charges

A problem common to all local authorities regardless of the adequacy of their revenue base is the lack of standards and guidelines for setting tax rates. This is true even for user charges and license fees, which all local authorities are allowed to levy. The need for some degree of rationality and standardization is evident. Without them, the local authorities may not only fail to recover costs and raise sufficient revenues to provide their services and repay their debt, but may also generate efficiency and equity effects.

A comprehensive review of all fees, charges, and taxes used by Kenyan local authorities should be undertaken by the Government of Kenya. On the basis of that review, the Ministry of Local Government should issue guidelines for local authorities to use in setting revenue rates and for the Ministry itself to use in considering revenue rate requests. License fees should be set within certain bounds that would vary by profession, type of local authority, and wealth of local authority. Many types of fees and charges in local authorities should be differentiated on the basis of size, location, or other business characteristics. Some local authorities already make liberal use of such distinctions, but others do not use them at all. As a result, merchants in city centers who are relatively wealthy and get substantial services may pay the same license fees as merchants in poorer rural areas, or large-scale traders may pay the same fees as small-scale traders.

Given the existence of unexplained fee differentials across certain professions and the possible underutilization or irrelevance of many types of fees, it would be desirable to simplify the fee and charge structure. Charges could be more standardized across comparable professions within local authorities, and fees that are unlikely to generate revenue could be removed from the schedule. These actions would reduce inequities in fee levels across professions as well as streamline the schedule of fees and charges. Another possibility might be to charge license fees on the basis of volume of business (in Kenyan Shillings) instead of type of profession or trade. Finally, some commercial and professional service providers are currently not required to pay any license fees, including wealthy professionals such as doctors and lawyers. This exclusion should be revoked because there is no good economic basis for it.

User charges should be set at least high enough to cover costs of service provision, interest charges, and replacement investment, unless there is adequate justification for the subsidization of particular services. The Government of Kenya should consider allowing local authorities to institute fees and charges for certain free services, such as health care, on an ability-to-pay basis, or the quality of health care provided by local authorities is likely to decline as the demand for their services continues to increase. In Nairobi, for example, the Director of Kenyatta National Hospital, the largest public health facility in the country, recently announced that adult patients should go to the clinics run by the Nairobi City Commission rather than to the hospital. The City Commission is not in a position to bear this financial responsibility without additional revenue. Longer-term fee and charge policies will require continued research and monitoring.

In order to set user charges properly, the Government should develop measures of cost effectiveness and standards for the provision of local authority services. These would also permit the identification of excessive spending on labor and materials for specific services, enabling action to be taken to adjust costs to a reasonable level. It is important to recognize that this may cause other problems. For example, many local authorities are likely to discover that they employ more people than they need for service provision. Although it may be politically difficult to dismiss excess staff, it may at least be possible to use them more productively in another position.

One last important point to make about setting tax rates, fees, and charges is that they must be revised on a regular basis unless they are ad valorem taxes. As noted in the previous chapter, the failure to revalue land regularly and to increase fixed fee charges is one of the chief causes of the inelasticity of the local authority tax base in Kenya. What has happened frequently in the past is that no increases were made for years. When the councils reach a point of desperation and try to raise the rates or fees by a large percentage all at once, there is tremendous political opposition, which prevents the increases from passing the councils, and leaves the local authorities in a desperate financial condition. Some fixed-fee local taxes could be made ad valorem, while others could be indexed to the increase in consumer prices. These measures would increase the elasticity of the local tax base substantially.

Raising Revenue From Nonresident Service Beneficiaries

The Government of Kenya should investigate the possibility of instituting some mechanism for local authorities to recover revenue for services provided to the residents of other jurisdictions. The current situation is not efficient in some places because nonresidents use the services of local authorities without paying for them. Possible solutions could include a fee system, a tax that would fall on nonresidents who use services, or a compensatory grant from the central government. The simplest solution for general cost recovery would be to allow a small local sales tax. This would be easy to collect and would cover retail activity in the formal sector that escapes market and trading fees. In cases where it is possible, such as health care, fees should be charged for the use of specific services.

Alternative Sources of Revenue

Even if existing revenue sources were more generally allowed to local authorities and they were able to improve their current revenue collection problems greatly, some local authorities would not have enough revenue to provide adequate public services and to deal with their outstanding debt. There are a number of potential revenue sources that are not being exploited by local authorities, which could greatly improve their financial position. If the local authorities are ever going to be strengthened into entities capable of doing a substantially better job of providing public services, many will need to have access to additional sources of revenue. In order to diversify the local revenue base, the Ministry should consider the introduction of additional revenue sources to local authorities where appropriate. This will require substantial research, including an examination of the potential revenue yield of alternative taxes as well as their potential efficiency and equity effects. This section will suggest some options for alternative sources of revenue that should be considered.

There is strong support among local authority officials for revival of the Graduated Personal Tax (GPT) or the institution of a new local payroll tax. This would greatly enhance the revenue capacity of all types of councils, but would largely benefit the urban areas where the formal sector is important. It is an easy tax to administer because collection is done by employers, and in its previous form, it was a criminal offense not to pay it, so there was good compliance.

At the request of the Ministry of Local Government, the Cabinet has approved the institution of a new tax called the local service levy, which is similar to the old GPT. This is a small, roughly proportional local tax on those who have an identifiable source of income over a minimum level.[3] Cabinet Paper CAB (87) 33 of April 1987 suggested that initial rates should range from 10 shillings per month for those with a gross monthly income of 700 shillings to 100 shillings per month for those earning over 6000 shillings.

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[3] The original intention of the Ministry of Local Government was to have a modestly progressive tax on income, but this idea was dropped because it was considered to be politically unacceptable.

The Cabinet paper leaves open the possibility that local authorities could vary from this modest scale with the approval of the Minister for Local Government, and the scale could be raised over time. This tax will significantly enhance the revenue base of councils in urban areas. The tax will particularly benefit Nairobi, which is expected to raise more than 5 million pounds from it annually. The tax is so small that it should not cause any significant distortions in behavior. Although it has been approved, the tax is not yet in use.

In response to the MLG Cabinet paper on the local service levy, the Cabinet recommended that some form of the local service tax be applied to businesses. The MLG is tentatively suggesting that a development levy of 0.1 percent of authorized share capital or total assets of businesses be instituted by local authorities. This matter requires further study because businesses are already relatively heavily taxed by local authority land rates, at least in the larger cities, so that the proposed development levy is a form of double taxation. In addition, authorized share capital may not be an appropriate measure of either business ability-to-pay taxes or use of local services. Finally, such a tax may be deductible from the profit and loss account of businesses, thereby reducing the base on which Government's corporation tax is levied. If an additional local tax on business is to be instituted, it may be preferable to allow a small local add-on to Government's corporations or sales tax.

One important source of revenue often underutilized in certain areas is tourist activity. Tourism is the lifeblood of some local authorities in the way that agriculture or industry is in others, yet local authorities have no access to tourist-related taxes in many areas. It is true that county councils with game reserves in their jurisdiction can get significant revenues from entrance fees, but this is only true where the game reserves belong to the councils. National park revenue belongs to the central government, and local authorities get little or no revenue benefit despite the fact that they bear some of the service burden generated by tourism. The bed occupancy tax is fully under the control of the central government, so that local authorities get little more than meager license fees once a year from tourist hotels. Although tourism generates a great deal of economic activity in some areas, it generates negative externalities as well. Tourist resort areas in the Coast Province, for example, may place heavy service demands on local authorities but generate little revenue. Some form of local authority tourist tax would help to redress this highly inequitable and inefficient situation. A tourist tax also has the advantage of allowing local authorities to export a portion of their tax burden to nonresidents, who in this case are often relatively wealthy foreigners. The most logical option would be a local add-on to the central government bed occupancy tax.

Allowing more local authorities to be water providers, to the extent it is feasible to do so, would enhance their revenue capacity, as would more widespread use of other revenue-generating activities, such as housing estates, slaughterhouses, busparks, and hotels. In some districts, it would be possible to develop new game reserves as a source of revenue for county councils.

There are also a number of other smaller or special sources of revenue that have not been tapped by some local authorities. Charges for parking fees and other automobile-related taxes in more urban areas are one example. Others might include grazing fees for livestock and special assessments for specific capital projects in areas where there is ability to pay for such projects. An example of the latter would be apportioning some of the costs of road development to adjacent plot owners, which has been done successfully in some areas of Nairobi.

An alternative approach to allowing local authorities some of the above sources of revenue would be to allow them the option of adding some small local percentage to central government taxes. As long as the existing central government tax rates are relatively low, a small local add-on by local authorities will not be very distortive, and would be very productive for local authorities; furthermore, centralized collection is, in many cases, more administratively efficient than local collection. One possibility might be to allow local authorities to add a small percentage to the national sales tax. Another possibility would be to allow local authorities a small percentage of the motor vehicle license fees and/or the motor fuel tax. Some portion of this revenue could be used for road construction and maintenance, a costly service which most local authorities do not have the resources to provide adequately.

Local authorities obviously do not need access to all of the sources of income discussed in this section, but some new sources are certainly appropriate for many of the councils. The Government of Kenya needs to review its priorities and decide on some options that provide reliable sources of revenue for local authorities and are efficient, equitable, and politically feasible to implement.

Intergovernmental Institutional Reforms

A number of intergovernmental institutional problems were discussed in the previous chapter. These take a variety of forms. In some cases there is a failure of particular agencies or authorities to live up to their responsibilities, resulting in operational difficulties for local government. There are also problems with poorly defined intergovernmental relationships and significant unexploited opportunities for intergovernmental cooperation. These intergovernmental institutional problems contribute to the poor fiscal performance of local authorities in Kenya.

In order to provide local services adequately and efficiently, institutional reforms will have to be implemented at all levels. The entire integrated intergovernmental system has to operate in a coordinated manner. The central government ministries that monitor and/or assist specific aspects of local government operations must function efficiently, and the provincial/district administration under the Office of the President must ensure that the decentralized activities of the ministries and the local authorities are coordinated and in support of national development goals. In addition, the local authorities should be able to work formally with each other on the provision of specific services in order to improve efficiency. Finally, fiscal operations in the local authorities, where the services are actually delivered, must conform to some minimum standards. Intergovernmental institutional reforms are discussed in this section, while local institutional reforms are examined in the next section.

Local Authority Interjurisdictional Cooperation

The lack of intergovernmental cooperation among local authorities was described in the previous chapter. The Government of Kenya should encourage local authorities to take advantage of the provisions in the Local Government Act that allow them jointly to provide mutually beneficial services. Most local authority officials are aware of these provisions, but seem reluctant to take advantage of them even when there are situations in which their councils could clearly benefit from them. It is up to the Ministry of Local Government to take the lead in educating local authority officers about the possibilities and procedures for exploiting the opportunities available to them in the interests of greater efficiency. It would be possible to devise some incentives to encourage interjurisdictional cooperation in cases where it is appropriate.

It would also be efficient in some cases to use the regional development authorities to facilitate the provision of certain services over multiple local authority jurisdictions. Water, for example, is a service that could be more efficiently provided in certain areas by a regional authority because of scale considerations and externalities. Local authorities might be directly involved at some level, or their participation might be confined to payments to the regional authority for services rendered. Some additional regional development authorities may need to be created to serve areas where they do not currently exist.

Ministry of Local Government

The previous chapter explained how the Ministry of Local Government (MLG) generates a number of serious constraints on the functioning of local authorities in Kenya.

The need for the MLG to standardize guidelines for assigning revenue sources and setting tax rates and charges has already been discussed in this chapter. In addition, there are many other steps that could be taken to improve the functioning of local authorities as well as the efficiency of MLG operations.

The Government of Kenya should improve staffing and training in the MLG to facilitate more rapid and standardized processing of local government requests and submissions regarding budget estimates, schedules of fees and charges, by-laws, employment decisions, etc. There should be clear designation of MLG officials with responsibility for particular geographic and substantive areas. Local authority officers should know exactly whom they should see about specific problems and requests.

Some MLG junior officers clearly know very little about how local authorities work and what their problems are. This situation could be improved by establishing a program to acquaint newer and less-experienced members of the MLG staff better with how the local authorities operate on a day-to-day basis. They could be sent to work in local authorities for a specified time period to work first-hand with local authority officers. Alternatively, local authority officers, who are now civil servants under the jurisdiction of the Public Service Commission, could be brought to Nairobi to work in the MLG for a period of time.

To the extent permitted by the Local Government Act, there should be greater delegation of authority both within the MLG and between the MLG and the PLGO/local authorities. This will allow for greater administrative efficiency in both the MLG and the local authorities. It may be necessary to consider options for reforming the Local Government Act over the long term because some of the provisions of the Act can be conservatively interpreted to proscribe meaningful decentralization. The Government of Kenya is supposed to be in the process of setting up an interministerial committee to investigate the need for reforms in the Local Government Act.

The MLG urgently needs to institute a simplified and standardized accounting code for local authorities. The current system tends to be complex, but varies significantly across local authorities and even for some individual local authorities over time, making analysis and comparisons across councils and across time very difficult. A new system will take time to develop fully, but its design can begin immediately. The World Bank is ready to provide the funds for such an exercise, which is currently in the planning stages at the MLG.

The MLG should use the new accounting system to develop a time-series database on local authority finances. This type of information will facilitate the work of the Ministry in monitoring the financial position of local authorities, developing guidelines for setting tax rates and charges, and establishing revenue collection targets for the councils. The evidence collected in this research suggests that some local authority revenue sources are highly inelastic or unstable and that costs of service provision vary dramatically across councils, but these issues need to be understood better through formal analyses of time-series data.

Finally, a Research Section should be established in the Ministry of Local Government to supervise the collection and monitoring of local authority data and to provide ongoing research support to the Finance and Planning Sections. The Ministry may need outside technical assistance for some of its research, while it builds up its own capacity, but this should be coordinated with the Ministry's own work and supervised by Ministry officers.

Other Ministries and Provincial Administration

The problems that other central government ministries and offices can raise for local authorities were discussed in the previous chapter. The central government can only deal with this situation by insisting that operating ministries on which local authorities are dependent for planning, engineering, and other technical expertise fulfill their responsibilities in a timely fashion. If the President mentioned the issue just once in a speech, the offending ministries would be frantically working on rectifying the situation the next day. Some of these ministries are plagued by persistent resource shortages that prevent them from meeting their responsibilities to local authorities, so that it may be necessary for the central government to provide additional support. Over the longer term, a better solution is to build up the technical capacity of the local authorities, but this will not eliminate the need for the local authorities to depend on other ministries and offices to some extent. Local authorities are required by acts of Parliament, for example, to obtain permission from certain ministries before they undertake particular activities, and they must also obtain approval of their by-laws from the Attorney General.

In recent years, there has been much closer interaction between local authorities and the provincial administration because of the District Focus for Rural Development strategy, but much more effort needs to be made in this direction. No matter how they feel about District Focus, the local authorities must accept the fact that it is now the way things work. Also, they should realize that there are certain important advantages to having a close relationship with the provincial administration, and that the goal of coordinating all development projects in the districts is a worthy one.

There is a lot of unrealized potential in the District Focus strategy, and the central government should try to tap it. There is a need for greater clarification of the relationship between local authorities and the District Development Committees, and a well-articulated set of guidelines for inter-council cooperation and coordination should be developed. The DDCs could also help local authorities with financing certain types of projects. This issue, however, needs to be thought out carefully, or problems could result. If the DDC undertakes the funding of selected local authority projects, it must do so in a way that does not foster an unhealthy degree of competition among local authorities for limited project funds.

If a more effective and well-defined role for the DDCs vis-a-vis local authorities can be developed, great benefits for both the local authorities and the districts may be realized. In addition to providing intradistrict coordination of development activities, the DDC should ensure that these activities are consistent with national development goals and strategies. This is particularly important as the Government of Kenya prepares to initiate the District Development Fund and to begin implementation of the rural-urban balance strategy outlined in Sessional Paper No. 1 of 1986 and discussed in Chapter 4.

Intergovernmental Grants

Even if local authorities improved revenue collection and were granted additional sources of revenue, there remains one issue that the Government of Kenya has not attempted to solve: some local authorities are so impoverished and have so few types of economic activity that they will remain in poor financial shape even with improved administration and new sources of revenue. Although there are grants to needy councils provided by the MLG for some of the very poorest councils, there is no systematic way of measuring such need and channeling grant funds to these councils. In the interests of equity and to guarantee basic service provision, a system needs to be developed to allocate the scarce grant resources of the MLG to those local authorities who need it most. In the absence of such a system, the likelihood of using such grants for political favors is greatly increased. In addition, the grants currently being given to needy local authorities are in many cases only nominal sums that do not go very far in helping these local authorities solve their revenue problems.

The needed intergovernmental aid system could be designed in a variety of ways. It might, for example, be a transfer program that provides direct grants to local authorities from central government revenues on the basis of a formula that rewards tax effort and limited fiscal capacity. Alternatively, there could be a tax-sharing system whereby a certain percentage of a national tax or taxes is remitted to local authorities according to some reasonable distribution criteria.

It is well recognized that the resources of the GOK are limited, and that Sessional Paper #1 of 1986 has outlined plans to channel funds to areas in local authorities designated as Rural Trade and Production Centers. The idea of intensively developing infrastructure in high potential areas is an excellent one because of its expected impact on overall economic development, but it does not lessen the need to do something about the poorest councils. Additional resources need to be identified for grants to needy local authorities if these grants are to have any meaningful impact.

Local Government Debt

This study has not closely examined levels of debt outstanding or repayment records of local authorities. Good data on this are difficult to get because of the way in which the Local Government Loans Authority keeps its records and the reluctance of many local authority officials to discuss the topic in detail. LGLA accounts are currently being updated, but the information is incomplete and confidential. Available evidence indicates that total outstanding local authority debts to the LGLA exceed two billion Kenyan shillings, at least several hundred million of which are in arrears. About 89 percent of this debt is estimated to be held by fewer than 20 municipal councils. Many of the indebted local authorities have made little or no attempt to repay.

The Government of Kenya should begin to think about devising a reasonable plan for dealing with the local authority debt problem. Forcing local authorities to pay back their loans fully to the Local Government Loans Authority is not necessarily the solution to the problem, and it may not even be possible. Even if they improved revenue collection and were granted new sources of revenue, local authorities might use a high percentage of the additional income on debt repayments for a significant period of time if they were forced to repay too quickly. Residents of the local authority would be paying higher taxes, but at least for some period of time, perhaps see few benefits in the form of improved and/or expanded services. This could create local political problems.

It should be recognized that many of the outstanding loans to local governments are old and were the result of the poor planning, lack of management skills, and perhaps dishonesty of local authority and/or Government officials who may have retired or changed jobs long ago. There is also the issue that local authorities are owed large sums of money by Government and parastatals. The financial claims of both sides are in some cases so enormous that full repayment on either side may be extremely difficult. It seems likely, therefore, that Government may at some point need to work out a loan forgiveness and/or rescheduling plan that is fair to all parties.

Any type of loan forgiveness or rescheduling scheme must be designed very carefully, however, so as not to reward those local authorities that can be proven to have been negligent and/or dishonest. In some cases, it is certainly true that loans have not been repaid for reasons beyond the control of local authority officials despite their good intentions. Any scheme for loan forgiveness or rescheduling should reward those councils that have done their best to service their debt and, at the very least, not penalize those that have been unable to pay. In some cases, however, it may be possible to demonstrate that some relatively well-off councils have failed to make payments due to negligence or corruption, and these councils should be dealt with more severely.

Some elements of the donor community interested in strengthening local authorities might consider the possibility of devising an arrangement for helping to repay central government and/or parastatal debts to local authorities on the condition that local authorities then repay their debts to the central government. This could be done, for example, by attaching a conditionality to a new loan made by a donor to the Government of Kenya. Before the loan is applied for its intended purpose, the central government could use the funds to settle its debts and perhaps those of the parastatals to the local authorities in full or up to some amount to be decided on in the case of a particular local authority. The local authorities would be required to use these funds for the purpose of settling their outstanding debts to the Local Government Loans Authority and other central government institutions to which it is indebted. The LGLA would not be allowed to use any of these funds that are owed to the central government--they would be immediately credited to outstanding LGLA loan accounts with the Treasury.

A plan of this nature would not completely erase the debt problem because some local authorities may owe the central government more than the central government owes them, and vice versa. It would, however, reduce the magnitude of intergovernmental claims, put many local authorities in a better financial position, and help to recapitalize the Local Government Loans Authority or the institution that replaces it. The local authorities, the central government, and the parastatals would still have various claims on each other, but the only case in which debt would have increased would be that the parastatals would owe more money to the central government to the extent that some of their debts to local authorities had been paid with money lent to the Treasury.

In order to design and implement a plan of this nature, the government needs to have better data on the local authority/central government/parastatal mutual indebtedness problem. Efforts should be made to quantify as accurately as possible other local authority debts as well as central government and parastatal debts to local authorities.

Sessional Paper No. 1 of 1986 calls for the reorganization of the Local Government Loans Authority into a Municipal Development Bank. Although existing debt problems urgently need to be dealt with first, recapitalizing and strengthening the institution that funds most local authority capital projects is an important and necessary goal. The credibility of the agency that supports local authority investment should be re-established.

The MLG is likely to recommend that the new institution be established under the Companies and Banking Acts. A privately held and commercially viable institution would be able to attract private capital, increasing the pool of capital resources available to local authorities and taking some of the burden of financing local authority investment from the central government. Offering loans at closer to commercial rates than at present would force local authorities to take on projects with a higher rate of return and encourage timely repayment by raising the penalty for defaulters. Although it is unlikely that local authorities as a group will be able to generate substantial net savings, at least in the short term, commercial rates may stimulate local authority savings to some extent. Even short-term savings would earn interest for local authorities and provide funds to loan to other local authorities.

The new local authority lending institution should only finance commercially viable projects. Of course, some necessary local authority projects are not going to be self-financing, and there should be central government provisions for lower cost loans or grants for these types of projects. The District Development Fund, which was set up with donor money to fund projects in support of the rural-urban balance strategy, is one possible source of funds for nonbankable projects. Recent experience suggests that additional donor funds are likely to be available for such purposes.

Local Institutional Reform

The previous chapter emphasized the degree to which local institutional problems have a negative impact on the performance of local authorities. This section will recommend some policies for alleviating obstacles to the efficient operation of local authorities caused by local institutional deficiencies.

General Reforms

The numerous administrative and managerial problems of local authorities that constrain their fiscal activities were briefly outlined in Chapter 6. Whatever other steps the Government of Kenya may take to strengthen local authorities, it will be necessary to deal with administrative and managerial constraints if the local authorities are going to be able to operate effectively. Some of the needed reforms can be initiated by local authorities, but support and incentives from the central government are likely to be required in many cases.

As discussed in the previous section, accounting procedures in Kenyan local authorities are unnecessarily complex and diverse. They should be simplified and standardized to facilitate better financial management, so that reliable financial information is available. This implies that auditing of local authorities by the central government must also be conducted in a more timely fashion.

The Ministry of Local Government and the local authorities should jointly devise and institute better revenue and expenditure control management techniques, including budgeting and planning, cash flow management, and strengthening the role of the internal auditor. These procedures should be implemented on a rationally designed, step-by-step basis. There is no sense, for example, in requiring local authorities to prepare three-year forward budgets if they are still unable to prepare a single year's budget properly.

The Government of Kenya should intensify its efforts to train local authority officers and employees at all levels, and should formally institute relevant training for councillors as well. The training should be on-going and, in some cases, on-site in order to have the best possible impact. Incentives for promotion and advancement should also be implemented in an effort to increase staff productivity.

Reforming Revenue Collection

The difficulties of revenue collection are probably the most crippling of all local authority administrative problems. The Ministry and the local authorities should institute policies designed to strengthen local authority revenue collection and expand enforcement staff and techniques, including the solicitation of formal cooperation from the Kenya Police and the District Commissioner and the introduction of better collection and monitoring procedures. Institutionalized cooperation between the local authorities and properly empowered enforcement authorities could go a long way towards improving the revenue collection capabilities of the local authorities.

The pocketing of public funds by local authority employees could be somewhat reduced by hiring better screened and better trained collectors, rotating and monitoring collectors and enforcement officers, instituting better pay and bonus systems for more productive revenue collectors, and where possible, instituting checks on and control of the revenue-collection process. It would be extremely helpful to institute multiple record-keeping and cross-checking of receipts and records in areas where this is feasible. In many slaughterhouses, for example, there are at least three sets of records kept regarding the number of animals slaughtered--those of the slaughterhouse master, those of the operator who transports the animals to market, and those of the health inspector. All of these people charge on a per animal basis, and their records should be in exact agreement. In some cases there may be a fourth set of records if there is a local tannery. In general, it would be helpful to implement revenue control measures that require independent record-keeping by at least several individuals.

In order to help reduce corruption, the Ministry of Local Government should educate clerks and treasurers about MLG and Public Service Commission rules and regulations to encourage them to take action against dishonesty. The Ministry needs to assure local officers that they will be fully backed for doing everything in their power to take action against dishonesty at any level in their councils. Better internal auditing, revenue collection incentives, and more efficient monitoring of these types of situation by the MLG could help reduce the problem of dishonesty among the local authority officers themselves.

Local authorities clearly need stronger enforcement powers for land rates, and a local court system for local matters would greatly expedite local authority collection proceedings. The councils would also benefit from a pool of trained lawyers who had experience in land rate recovery cases. As many local authorities could not afford a full-time advocate, it might be possible for the MLG to retain a group of advocates, who could be hired out on a fee-for-service basis to the local authorities.

Reforming Intra-Council Relationships

The Ministry of Local Government should institute a system for greater monitoring of the relationship between local authority officers and elected councillors in order to deal with the problems in this area discussed in the previous chapter. One of the major problems is the exertion of political pressure for certain expenditures to be made or certain taxes not to be collected. Pressures for spending on favored activities will never be eliminated, but improved guidelines for project feasibility studies and evaluation, which are currently being developed and disseminated by the Ministry of Local Government's Planning Section, can help to some extent by formalizing procedures and standards for project selection. Better auditing and MLG review of projects might also help reduce inefficient spending. On the revenue generation side, some of the reforms discussed earlier, such as greater standardization of allowable revenue sources, explicit guidelines governing the periodic increase of tax rates, and better and more independent auditing, should reduce, to some extent, local political control over revenue collection.

A major issue is the lack of familiarity on the part of some councillors with important financial and administrative issues. There are several potential ways of dealing with this problem. One is to have minimum education or experience requirements for councillors, or at least for those who will chair the various major committees of the council. It must be acknowledged, however, that educated councillors are just as capable of causing problems for local authority officers as illiterate ones. Minimum education requirements obviously cannot be considered a panacea for tensions and misunderstandings between elected and appointed officials.

Another idea would be to offer a comprehensive training seminar for elected councillors to educate them on their responsibilities and powers as well as the role of their appointed officers. Some training of this nature has been experimented with by the Ministry of Local Government, but it raised a number of strong complaints from a few local authority officers. These officers claimed that some councillors came back with a misunderstanding of their role, and they tried to order the officers to do certain unreasonable things. In the opinion of the officers, the seminars for councillors created more problems than they alleviated. They argued that these seminars should actively involve local officers as well as councillors to reduce the probability of generating such frictions and misunderstandings.

In general, there seems to be a relatively productive and cooperative relationship between councillors and officers in many councils. It is clear, however, that there are a few problems that could be alleviated to a marked degree by greater discretion and patience on the part of some officers and councillors, the institution of a few new regulations, and the improvement of both the external and internal auditing procedures in local authorities.

Agenda for Additional Research

This chapter has raised a number of important research questions related to the fiscal role and operation of local authorities that the Government of Kenya needs to answer, related particularly to options for revenue generation, the reform of institutions that affect local government performance, and improving the administrative and managerial capacity of local authorities. In addition, there are a variety of other research topics that would provide useful information for the Government as it considers the problem of what to do about local authorities and some of the specific issues raised in this chapter.

One area of great interest is the overall financial position of local authorities, particularly how it is changing over time and how deficits are being financed. As noted in Chapter 4, recent evidence suggests that the financial position of some local authorities has been steadily deteriorating over time, and that deficits are frequently being financed by drawing down the balances of various types of separate fund accounts. The Ministry of Local Government needs to understand better the nature and extent of this problem if it is ever going to be able to design and implement significant measures to improve the situation.

A detailed comparison of estimated budget figures and actual revenue and expenditure figures across councils would also be extremely useful. The limited evidence collected in this study suggests that the two sets of figures often show very little similarity to each other. This indicates, at least in some cases, that the council budgets submitted to the Ministry for approval bear very little resemblance to reality. This type of misinformation can lead to poor decisions by the Ministry and continued problems in local authority finances.

Some measures of fiscal capacity and fiscal need should be developed for Kenyan local authorities. Only if revenue possibilities and expenditure requirements are understood more fully will it be possible to know which local authorities are truly able to finance service provision in their jurisdictions. For those local authorities who are financially unable to provide services, the Government of Kenya must decide whether it will provide grants to make up the income shortfall, transfer some services to a Government of Kenya ministry, or devise some other solution to the problem over the long term.

Summary of Major Reforms

The present system of local government in Kenya is plagued by a variety of deficiencies and constraints that undermine its effectiveness. Many of these problems are highly interrelated, so that attempts to make reforms in one area will be unsuccessful without reforms in related areas. Although some reforms are clearly more urgent than others, there are serious deficiencies in most aspects of the Kenyan system, requiring that many reforms be implemented more or less simultaneously in order to be effective. This section will summarize the major reforms that are needed and give a sense of their priority in the reform process.

The division of service responsibilities that has evolved between the central and local governments in Kenya is fairly reasonable on economic grounds. There are a few improvements and clarifications that should be made in service assignment, but for the most part, local authorities have a clear role to play. The exception to this is the county councils, which could be given the expanded and productive role of facilitating marketing and distribution within their districts. This should not be attempted, however, until local government fiscal and managerial capacity have been improved.

In spite of generally reasonable service assignment, a majority of local authorities are unable to fulfill their service responsibilities adequately because of a wide variety of constraints on their operation. The most significant problems are in the area of revenue generation. Although the revenue-expenditure correspondence is not very good in many rural councils, the councils in urban areas should have adequate resources to meet their requirements. In reality, this is often not the case because revenues in most local authorities frequently grow more slowly than service demands. There are tremendous obstacles to revenue collection, and tax rates, fees, and charges are rarely set in a rational and standardized manner; furthermore, local authorities do not have control over the sources of revenue that they are allowed to use. The end result of these problems is a revenue yield that is inadequate and a local tax system that has an inelastic base and violates principles of equity and efficiency to various degrees.

A number of steps could be taken to moderate the revenue problems of local authorities and some of their undesirable effects, the most important of which involve institutional and procedural reforms. Standardization of access to sources of income across local authorities and more general application of taxes within local authorities would help alleviate the problem of revenue inadequacy, lessen the dramatic differences in per capita spending across local authorities, and reduce efficiency and equity problems induced by the existing tax system.

Other reforms related to revenue generation should be implemented at the same time. More frequent revaluation of land, institution of selected ad valorem taxes, and periodic revisions or indexing of fixed-fee taxes and charges could substantially increase the elasticity of the local tax base. Unstable sources of revenue, such as cesses, are a more difficult problem to deal with, particularly in the short run and in rural areas. Over the long run, a movement towards greater reliance on land rates could improve the situation in a majority of local authorities.

After strengthening and standardizing existing sources of local authority revenue, the central government should turn to the issue of additional sources of revenue, which are likely to be necessary in many local authorities. This chapter has suggested a variety of specific options for new sources of revenue. The actual mix of revenue sources that should be used is a decision that needs to be made by the Government of Kenya. Before that can be done, more detailed research needs to be conducted on the revenue yield and potential effects of the options discussed here. Some sources will be appropriate for particular types of places, but not for others.

Capital financing is a problem that goes hand-in-hand with recurrent revenue deficiencies in the vast majority of

Kenyan local authorities. Many local authorities are not credit-worthy because of inadequate revenue bases and poor managerial capacity, which result in an inability to service existing debts and responsibly assume new ones. Measures to improve fiscal capacity have already been discussed, and steps to strengthen managerial capacity will be outlined below. The problem of existing local government debt to LGLA and central government/parastatal debt to local authorities must be dealt with by the Government of Kenya in a way that does not create undesirable incentives and discourage continued local authority capital investment. Also, the Local Government Loans Authority, the central government institution that provides most of the financing for local government capital projects, should be recapitalized and restructured so that it provides the additional resources required to meet the growing demand for local authority infrastructure investment, and so that it operates more effectively and efficiently.

An additional significant revenue problem for the local authorities with low fiscal capacities is the lack of intergovernmental aid, which has contributed to the enormous variations in expenditures and service quality across councils. More substantial block grants distributed according to a clearly defined and equitable formula would help to correct this situation. In some cases, grants might be given to ensure the provision of particular basic services.

Any significant reform of local authorities will have to deal with a number of major intergovernmental institutional problems that have plagued their fiscal performance. Greater efficiency in resource use could be attained if a number of institutional reforms were implemented. The arbitrary assignment of revenue sources by the Ministry of Local Government to local authorities has already been discussed. In addition, the MLG, which is supposed to supervise and assist local authorities, often constrains them in other ways as well. The Ministry has too much control over local authorities, and it is very centralized and inefficient in its own operations. There is a need for the Ministry to decentralize, to train its staff better, to be more aware of local authority problems and needs, and to provide greater support and technical assistance to the local authorities. Other ministries on which the local authorities critically depend for specific services or assistance should also be given the resources and incentives required to fulfill their responsibilities in a more timely and effective manner.

Local authorities themselves have not taken advantage of provisions in the Local Government Act that provide for intercouncil arrangements for service provision, despite the potential for such arrangements to increase efficiency in certain areas for particular services. The District

Development Committees also have a primary role to play in coordinating the development activities of central government ministries and local authorities within the districts. There is a great deal of potential for such coordination to lead to better-planned and more-efficient service provision, and efforts should be made to define the process more clearly than it is as present and to ensure that it is implemented more effectively.

Finally, a variety of local administrative and managerial problems stand in the way of effective local authority performance. These must be improved at the same time that the revenue reforms discussed above are being implemented. Enhanced revenue capacity and improved access to capital for local authority investment will be wasted without improved management and administration. Dealing with most of these local managerial and administrative problems is likely to require various degrees of central government assistance, ranging from simple guidelines to substantial technical assistance.

It is first necessary to institute standardized and simplified accounting and record-keeping systems. Better techniques for cash-flow management, revenue and expenditure control, and budgeting would also greatly improve the use of local resources. The introduction of a system of incentives and good training programs would increase the capacity and enhance the performance of local authority employees.

The local management problems with the most significant impact on local authority performance are in the area of revenue collection. Lack of collection and enforcement staff, inadequate enforcement authority, political pressure, and dishonesty are all major obstacles to better revenue collection, which could be alleviated to some extent by a variety of specific policies. Many of these problems are largely the result of insufficient resources, while others could be improved by correcting specific local institutional arrangements.

The conclusion that must be drawn from this analysis is that the current state of local authorities in Kenya is not very promising. However, even with all of its problems, Kenya probably has one of the most effective systems of local government service provision in Africa. The situation could be improved dramatically by a package of well-designed policies and interventions, which are aimed at removing major constraints on the effective fiscal operation of local authorities. A concerted effort should be made to strengthen not only the Ministry of Local Government and the local authorities, but also other ministries involved in local service provision and the District Development Committees, which coordinate local development activities. All of these institutions must have adequate authority and access to human and financial resources sufficient to discharge their responsibilities effectively. Greater decentralization would make the system generally more efficient and free up the MLG to monitor the local authorities more effectively than they currently do as the local authorities try to achieve a national standard in their performance. MLG staff time and resources should be concentrated on the places where they are most urgently needed, and those local authorities with good management and adequate capacity should be given additional autonomy.

Many of the policies and reforms discussed in this chapter will not be easy to define operationally and put into practice. Political constraints may even preclude a significant reform process in spite of the present rhetoric about strengthening local authorities. As discussed several times in this thesis, the type of support currently being expressed for local authority reform has been voiced on previous occasions without satisfying results.

If economic logic prevails over purely political considerations, reform may begin to proceed as soon as the middle of 1988, when the Minister for Finance presents his budget speech to the Parliament. If the reforms outlined here are accepted or others are devised by the Government of Kenya, some may have to be implemented on an experimental or incremental basis. If policies and reforms are shown to be successful in some areas, they can be expanded gradually to cover other local authorities, with the ultimate goal being the revitalization of the institution of local government in

Kenya. Success in this endeavour will require a serious commitment and cooperative effort from local authorities, the Ministry of Local Government, and the Government of Kenya, as well as additional support from the donor community.

CHAPTER 8

SUMMARY AND CONCLUSIONS: THE FISCAL ROLE OF LOCAL GOVERNMENT IN DEVELOPING COUNTRIES

Local government has not traditionally played a major fiscal role in most developing countries for a variety of reasons. Colonial powers often did not want to institute meaningful decentralized democracy because they feared losing control of their territories. Many of the countries that colonized Africa, Asia, and Latin America had centralized government systems at home, and these were more or less directly transferred to the colonies, but with an even more limited role for decentralized government in many cases. Even in developing countries where attempts were made to establish meaningful local government, local institutions often remained weak because local cultures accepted the foreign institutions slowly, and there was a lack of human and financial resources to develop them adequately.

The Future of Local Government in Developing Countries

Since obtaining independence, many developing countries have kept strong central governments. In some areas, this is due to cultural influences, but the major reason in many countries is a desire or perceived need to establish strong central control for purposes of stability and nation-building. Centralization is imposed in some developing countries largely to keep a particular tribe or newly established indigenous elite class firmly in control. Early development economists and planners supported the prerogatives of those in power by maintaining that centralized development was more efficient and could lead to higher rates of growth, creating income through multiplier effects that would eventually benefit the masses.

During the past ten years or so, there has been some turnaround in the tendency towards centralization in the developing world. Although governments in many developing countries are likely to remain highly centralized, there has been at least some explicit recognition that decentralization has definite benefits. This change in thinking has occurred for a number of reasons. First, centralized economic planning and development policies have not been very successful in many developing countries, and this has generated movements to institute decentralized decision-making processes and greater reliance on the market in pursuit of more efficient resource use. Second, worldwide economic conditions have created serious difficulties for developing countries, and this has prompted them to look to largely untapped local resources in the face of growing populations and public service demands. Third, more awareness by a better-educated population of the problems in their own countries as well as of events and conditions in the rest of the world has increased pressure on governments in developing countries to strengthen democratic institutions. Local governments, as agents of both decentralized decision-making and grassroots participation, have benefitted from this movement. It is likely that they will continue to grow in importance in many developing countries in the years to come.

Analyzing and Evaluating Local Government in Developing Countries

Despite the recent interest in strengthening local government in the developing world, the public finance literature has generated little new work in this area. This thesis has attempted to develop a basic framework for analyzing the fiscal role and operations of local government in developing countries through a detailed study of Kenya.

Analyzing an appropriate fiscal role for local government in developing countries is a difficult task for a variety of reasons, the major one being that countries in the underdeveloped world are extremely diverse. Although developing countries share certain common characteristics, there are substantial differences in degrees of development, dominant cultures, colonial histories, degrees of tribal/ethnic homogeneity, types of constitutions and forms of government, tenure as independent nations, and ways of organizing and operating institutions. All of these areas are highly related in the sense, for example, that the form of government and the way institutions are organized may depend on local customs, colonial history, and political climate.

As demonstrated in Chapter 2, the heterogeneity of developing countries in the above areas leads to significant differences in the organization and operation of their local government systems. There are different degrees of fiscal centralization of the public sector and different numbers of levels of decentralized government. There are varying degrees of political decentralization and grassroots participation, different assignments of service responsibility, and greatly varying fiscal capacities both within and across developing countries. Central governments in developing countries also differ widely in the extent to which they grant decentralized government autonomy in revenue-raising activities and the expenditure decision-making process. Many fiscal differences across local authorities in a particular developing country may be due to arbitrary and inconsistent decisions by the central government rather than decisions taken by the local authorities themselves.

As argued throughout this thesis, these differences make the process of analyzing local government in developing countries a somewhat eclectic exercise. There are standard rules that must be followed and institutions that must be considered in analyzing certain economic issues, such as international trade, monetary, and fiscal policies. The rules of the game are far less clearly defined when looking at the fiscal role of local government.

General Economic Principles

A basic economic theory of local government has been defined in the context of the developed countries. This was reviewed and its relevance for developing countries discussed in Chapter 3. Although there are some definite problems with trying to apply this theory to the underdeveloped nations, many of the basic principles set forth in it and economic theory in general should be followed in analyzing the fiscal role of local government in the developing world. Given the major political, institutional, and cultural differences between developed and developing countries and the extreme diversity along many dimensions across developing countries, however, each case must be analyzed and interpreted in its own particular context.

The general economic principles of adequacy, efficiency, and equity should guide any analysis of the fiscal role of local government in developing countries. A local revenue and expenditure system should be adequate to provide basic services and meet national and local goals as revealed through the political process. Efficiency in service provision requires that the public sector step in where the market fails to provide what the people want and that types and levels of public services correspond with the needs and preferences of the people, which may vary across space. Efficiency considerations also demand that the production costs of these services be as low as possible in terms of scale and factor proportions without adversely affecting the quality of services to a level unacceptable to the beneficiaries. Tax policies should be designed in order to minimize effects on people's decisions about the types and levels of economic activity that they engage in and where they do so. Finally, to as great an extent as possible, the principles of vertical, horizontal, and geographic equity should be respected.

Special Considerations in Developing Countries

As has been highlighted earlier, developing countries differ from the developed countries in a variety of significant ways that must be taken into consideration when analyzing the fiscal role of local government. If these factors are not taken into consideration, fallacious conclusions based on the experience of the developed nations will likely result. If attempts are made to implement policies based solely on these conclusions, they are probably doomed to fail, and they may generate additional problems.

Public Service Provision

A variety of special factors must be considered when analyzing the problem of service provision in developing countries. First, there is often an expanded role for the public sector to play in developing countries. Services that would normally be provided by the private sector in more developed countries, such as markets, slaughterhouses, and veterinary services, may have to be provided by the public sector in the developing world because of weaknesses in private institutions, scale considerations, and significant externalities.

As discussed in Chapter 3, preferences for types of public services could be either more or less homogeneous in developing countries than in developed countries, depending on whether there are wide variations in economic base and the degree to which such variations affect the mix of public services required as production inputs. Due to widespread poverty, however, preferences for levels of public services in developing countries are likely to be more homogeneous than in developed countries. People would be expected, for the most part, to be interested in the provision of a minimum level of basic public services rather than different levels of a wide variety of services. To the extent that preferences for types and levels of public services are relatively homogeneous, provision should be more centralized. Geographic isolation, however, may preclude centralization or regionalization of services. In addition, it may be more administratively efficient and politically expedient to keep certain services, which might by their nature warrant more centralized provision, at a decentralized level of government. Depending on the particular case, this may be a regional or local government.

Economies of scale and externality considerations must be taken into account when assigning services to different levels of government in developing countries. Economies of scale may suggest more centralized provision or the need for forming intergovernmental bodies to provide services across several decentralized units of government. The latter option is likely to require substantial central government intervention because of the general weakness of local authorities in developing countries. Externalities may be less important in developing countries because there are less-developed internal economic linkages and greater geographic isolation than in a developed economic system. More adequate infrastructure, however, can help to generate greater internal integration of the economy and may thus be seen as an important national development priority. Certain types of public services, such as inter-area highways that facilitate trade, for example, will generate positive externalities. In addition, there are special types of externalities that may be important in developing countries, such as those generated in the areas of human and veterinary health care because of the semi-nomadic lifestyle of some indigenous peoples.

Service provision in developing countries may be complicated by differences from the developed countries in the way local authority jurisdictions are defined. In developing countries, urban local governments may well have large areas under their jurisdiction that are actually rural and agricultural land. Similarly, some rural local governments may be responsible for the provision of urban public services in urban centers within their jurisdictions that are not separate local authorities. This heterogeneity of needs within some local authorities can greatly complicate service requirements.

Finally, there may be alternative arrangements for the provision of some types of services in many developing countries. Self-help movements, nongovernmental organizations, charities and religious institutions all have a significant role to play in service provision in many countries. These services should be coordinated by the government and taken into account when planning government expenditures. Although self-sufficiency is a long-term goal, local governments should certainly take existing and potential alternative service provision arrangements into account when planning the use of their own scarce resources.

Revenue Generation

Revenue-generation systems are extremely diverse across developing countries. In some cases, local authorities are responsible for raising all of their own revenue, while in other cases, they are almost entirely dependent on central government transfers. Different combinations of local and national revenues will make sense in different cases. The important consideration is to insure that revenues are adequate and appropriately based and that existing sources are as equitable and generate as few efficiency effects as possible.

Although different revenue-raising arrangements will be required in different situations, there is likely to be a more important role for central government transfers and loans to local governments in developing countries. Some local authorities in these countries are located in remote areas where few opportunities for economic activities exist. Without central assistance, they are unlikely to be able to function in any meaningful way. Possibly the most important revenue area for central government intervention is capital financing. Few local authorities in developing countries are likely to be considered eligible for commercial credit, and they probably could not afford it even if they were. Thus, the central government may have a vital role to play in helping to finance local government investment expenditures.

To the extent that local authorities in developing countries rely heavily on the central government for transfers, difficult choices may have to be made because the problem of scarce resources is likely to be more severe than in developed countries. The central government, in its attempt to achieve national development goals, may have to concentrate its limited resources in areas where they will be most efficiently and productively employed, rather than using grant revenues to effect greater equalization of local fiscal capacities. This suggests that there may need to be a nonuniform, asymmetric application of resources across local authorities, leaving some in much better shape than others.

In many developing countries, there is likely to be a problem with general coverage of economic activity by the local tax system. The sources of local revenue currently employed may be in use largely because of convenience or because they were inherited from a colonial administration, rather than because they were selected as part of a well-designed local tax system. This may lead to efficiency and equity problems, as well as a lack of correspondence between expenditure responsibilities and revenue-generating capacity. There is likely to be a need for reforming local resource mobilization practices in many developing countries.

Local government in developing countries may have access to additional sources of revenue because of their possible expanded functions and the role of other service providers discussed above. Markets, slaughterhouses, stock auction yards, and similar economic bases may be major sources of revenue in some areas. In addition, income, labor, and materials may be available through self-help movements and nongovernmental organizations. Such resources can greatly alleviate local resource constraints, especially if they are explicitly taken account of in the local government planning and budgeting process.

Nature of the Economy and Resource Considerations

The nature of the economy has an important effect on the types of public services required by the population and the sources of income available to local authorities. As was shown in the Kenya case, the local economic base determines whether residents primarily need urban services, agricultural services, or livestock services. Diversities in economic base also have an important effect on the types of revenue that the local authority can raise. The nature of the local economy may even preclude a viable local public sector funded from local sources. If the local economy is dominated by barter transactions or if the revenue bases are highly mobile, for example, it will be inefficient, and perhaps impossible, to levy a monetary sales tax.

Human and financial resource constraints also have a major impact on what functions a local government can undertake. Financial constraints can be alleviated by transfers if the central government or the donor community is in a position to provide them. Lack of technical and financial expertise on the part of local government managers and employees is a much more difficult problem to overcome. Different solutions, such as centralization of services, central government or donor provision of technical expertise, and the development of training programmes, will be appropriate in different situations and over different time periods.

Institutional Considerations

The structure of national and local institutions must be well understood when analyzing the fiscal role of local government in developing countries. Institutions are difficult to change and may be impossible to work around effectively, largely because political forces use institutions to maintain the status quo, no matter how inefficient or inequitable. In some cases, however, internal and intergovernmental institutional reforms in the realm of the possible could go a long way towards improving the functioning of local government.

The deficiencies of local government institutions and their tendency not to take advantage of possibilities for interjurisdictional cooperation have already been discussed. The existence of these deficiencies often dictates that there be greater monitoring and stronger control of local government by central government institutions in developing countries than might be justified in the developed countries. However, in some cases, such as Kenya, the degree of control is so great and its administration so inefficient that the central government probably makes the situation worse than it would be if local government were left on its own. A balance must be struck between local autonomy and central control, and this will vary across countries at different stages of development and with different capacities.

Local government in developing countries is also likely to rely on a variety of institutions of higher levels of government for technical assistance, at least until local capacity is built up over time. This being the case, it is important that these more centralized institutions do as much as they can to provide quality assistance in a timely fashion. Their failure to do so can cripple local authority performance.

In some developing countries, local authorities are not even important actors in an integrated multi-tiered system of government. They often exist alongside decentralized offices or agencies of the central government within the same geographic boundaries. In such cases, the central government agencies may have greater responsibilities and access to more productive sources of revenue than the local authorities. In these situations, it is appropriate to question whether the local authorities should be abolished or strengthened, and the answer may well differ in different cases. It is the responsibility of the central government to see that all levels of government have a productive role and commensurate power defined on reasonable and defensible grounds. In addition, it is normally appropriate for the central government to be responsible for coordinating the development and service activities of these various levels of government.

Local inadequacies in technical and administrative capacity, as discussed above, are likely to be important constraints in most developing countries. There are also other local issues that greatly affect the ability of local authorities to discharge their responsibilities properly. In particular, many local authorities in developing countries do not have reasonable administrative procedures and accounting/recordkeeping systems. This is, in part, a result of poor training and central government regulations, but it is also partially due to the inertia of local government managers and their unwillingness to change the way things are done. Administrative procedures and accounting systems should be simple and appropriate to the local circumstances.

In addition, inadequate personnel policies may lead to a great deal of waste and inertia among local employees. Poor pay and benefits, lack of clear goals and standards for promotion, and a scarcity of incentives may lead to poor employee performance, which translates into inadequate service provision and significant undercollection of revenues. Many of these issues could be dealt with by local action, at least to some extent, in most developing countries.

Cultural Considerations

Cultural factors must also be taken into consideration when analyzing the fiscal role of local government in developing countries. The nature and extent of cultural effects are likely to vary dramatically across developing countries. In some places, their effect may be highly significant, while in others it may be negligible.

Some cultural factors may have a general effect on the possibilities for developing local government institutions in developing countries. It was noted in Chapter 2, for example, that some Asian cultures tend to be authority-oriented and provide an ideal climate for a highly centralized government system. In contrast, many African cultures have a long history of some form of local self-government and should be more culturally receptive to the development of participatory local government institutions.

Other cultural factors may affect specific aspects of the local government system and interpretation of the theories traditionally used by economists to analyze them. A few examples will illustrate this point. The idea of individual preferences versus social preferences was discussed in Chapter 3. To the extent that social responsibilities to family, tribe, and homeland are more significant than individual preferences for moving to another location to improve one's standard of living, mobility may be less important than in the developed countries. Thus, the relevance of the proscription on decentralized redistributional policies for mobility reasons and the importance of Tiebout-type behavior may be significantly diminished. Cultural factors can also affect service demands and the appropriateness of particular tax bases. If livestock or land, for example, have a particular religious or cultural significance to a certain tribe or ethnic group, attempts by the local government to tax these bases may be contentious and/or futile. On the other hand, religious taxes may be an effective means to raise revenue in some countries. Finally, if behavior that is considered corrupt in western societies is culturally acceptable in some developing countries, this must be taken into consideration when analyzing local government systems. There are also many other ways in which cultural factors could influence the organization and operation of local government in developing countries.

Political Considerations

Political factors are often the most important constraints on local government in developing countries, and they often greatly influence the other areas discussed above. Many developing countries are politically immature. Their lack of political stability creates an atmosphere in which meaningful decentralization may be very difficult. As was argued in the case of Kenya, however, it is probably possible in many developing countries to strengthen local government without any threat whatsoever to the stability of the central government or to the power of the ruling groups. The need for political stability may easily be used as an excuse for maintaining the current regime, which may have its basis in the military, a particular dominant tribe or ethnic group that does not wish to share power, or a newly emerging indigenous elite who do not wish to share their wealth. Clearly, strong political forces can effectively block decentralization.

The central government may reserve a particular public service or source of revenue for its own use even when it is not necessarily appropriate to do so. The central government, for example, may keep most or all of the most productive and elastic sources of revenue for itself and leave the less-desirable ones for local governments. There may be ideological or political motives for the central government to maintain full control over certain important service functions, as was argued to be the case with education in Kenya. In such cases, there may be few prospects for genuine reform of the practice in question.

Local political considerations may also have an important effect on the fiscal role of local government. Although this is true to some extent in developed countries, the possibilities for abusing the system for personal and social gain are likely to be greater in developing countries than in developed countries because of poorly developed institutions and inadequately enforced laws and regulations.

Even if the guilty parties are caught in the act, justice may not be served and there will be no deterrent to others who want to do the same thing. There may be actions by local politicians leading to spending not in the public interest, as well as pressures on local authority officers not to collect the revenue that is due to them. These activities can greatly undermine the effectiveness of local authorities.

Research Considerations

When conducting research on the fiscal role of local government in developing countries, it is important to be aware of certain conditions and situations related to the research environment that may differ from or be more extreme than in the developed countries. Probably the most important of these is the realization that most developing countries are unitary states, which are fairly recent creations. They are politically as well as economically underdeveloped, and the issue of decentralization is a sensitive one. Thus, the research must be conducted in a manner that reflects an awareness of the sensitivities involved. Even if this is done, there may be changes in political climate that affect the work and over which the researcher has absolutely no control.

It is also important to recognize that procedures and facilities taken for granted in the developed countries may not be available in the developing world. It may take some time to locate documents in complex and antiquated filing systems even in the central government ministries, and photocopying facilities may not be available to facilitate retrieval of information. Telephones, good roads, reliable public transportation, and basic lodging may not exist in some areas, and local governments may be very geographically dispersed, complicating the process of scheduling and meeting appointments with local authority officials. Cultural barriers and general suspicion of strangers may hinder the prospects for good access to and reliable information from local authority officials, particularly if the researcher is a foreigner.

Finally, there are likely to be serious difficulties in comparing data collected from different local authorities in the same country. This is also a problem in some of the developed countries, but the situation in developing countries is likely to be more severe. The central government may not keep any information on local authorities, and there may be very different systems for keeping financial information in different local authorities. Financial years, income and expenditure categories, and levels of aggregation may differ dramatically across local authorities, and any of these may differ over time for individual local authorities.

For all of these reasons, doing research on local government in developing countries requires careful preparation in advance of starting the fieldwork. It is important to have a good sense of the political climate, relevant cultural factors, and deficiencies or bottlenecks in institutions, procedures, infrastructure, and facilities, all of which may affect the research substantially.

Conclusion

Analyzing the fiscal role of local government in a developing country is an interesting and challenging undertaking because of the current interest in the topic and the lack of research attention that has been paid to it. There are certain problems in using the economic theory of local government as the basis for analysis because it was developed in the context of the developed countries. Nevertheless, the economic theory of local government and public finance theory provide a set of basic generalizable principles, which can be used as a starting point for the analysis.

Despite the general applicability of economic theory, there is a need to take a much more interdisciplinary approach to analyzing the fiscal role of local government in both developed and developing countries. Analyzing the economic role of decentralized government is much more constrained by political and cultural factors than is the analysis of some other economic topics and institutions, such as macroeconomic policy and international trade management. The importance of context in analyzing the fiscal role of decentralized institutions cannot be overemphasized, particularly in less-developed countries. There are significant differences between the developed and developing countries, and contextual factors relevant to local government organization and performance vary dramatically across developing countries as well. Although general economic principles can be used as one basis for analysis, a much more comprehensive framework encompassing a wide variety of other contextual factors is required to assess realistically an appropriate fiscal role for local government in a particular developing country.

APPENDIX I

LOCAL AUTHORITY SITE VISITS[1]

Local Authority	Type of Council	District	Province
Bungoma	County	Bungoma	Western
Gusii	County	Kisii	Nyanza
Isiolo	County	Isiolo	Eastern
Kipsigis	County	Kericho	Rift Valley
Lamu	County	Lamu	Coast
Mandera	County	Mandera	Northeastern
Marsabit	County	Marsabit	Eastern
Meru	County	Meru	Eastern
Muranga	County	Muranga	Central
Nakuru	County	Nakuru	Rift Valley
Samburu	County	Samburu	Rift Valley
Turkana	County	Turkana	Rift Valley
Wareng	County	Uasin Gishu	Rift Valley
Bungoma	Municipal	Bungoma	Western
Eldoret	Municipal	Uasin Gishu	Rift Valley
Embu	Municipal	Embu	Eastern
Kericho	Municipal	Kericho	Rift Valley
Kisii	Municipal	Kisii	Nyanza

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[1] These local authorities were visited as part of the fieldwork conducted for this research. Some local authority names are listed as both county and municipal councils. Large urban areas in particular districts are often designated as municipal councils and have the same name as the county council. In Bungoma District, for example, two councils were visited, Bungoma County Council and Bungoma Municpal Council.

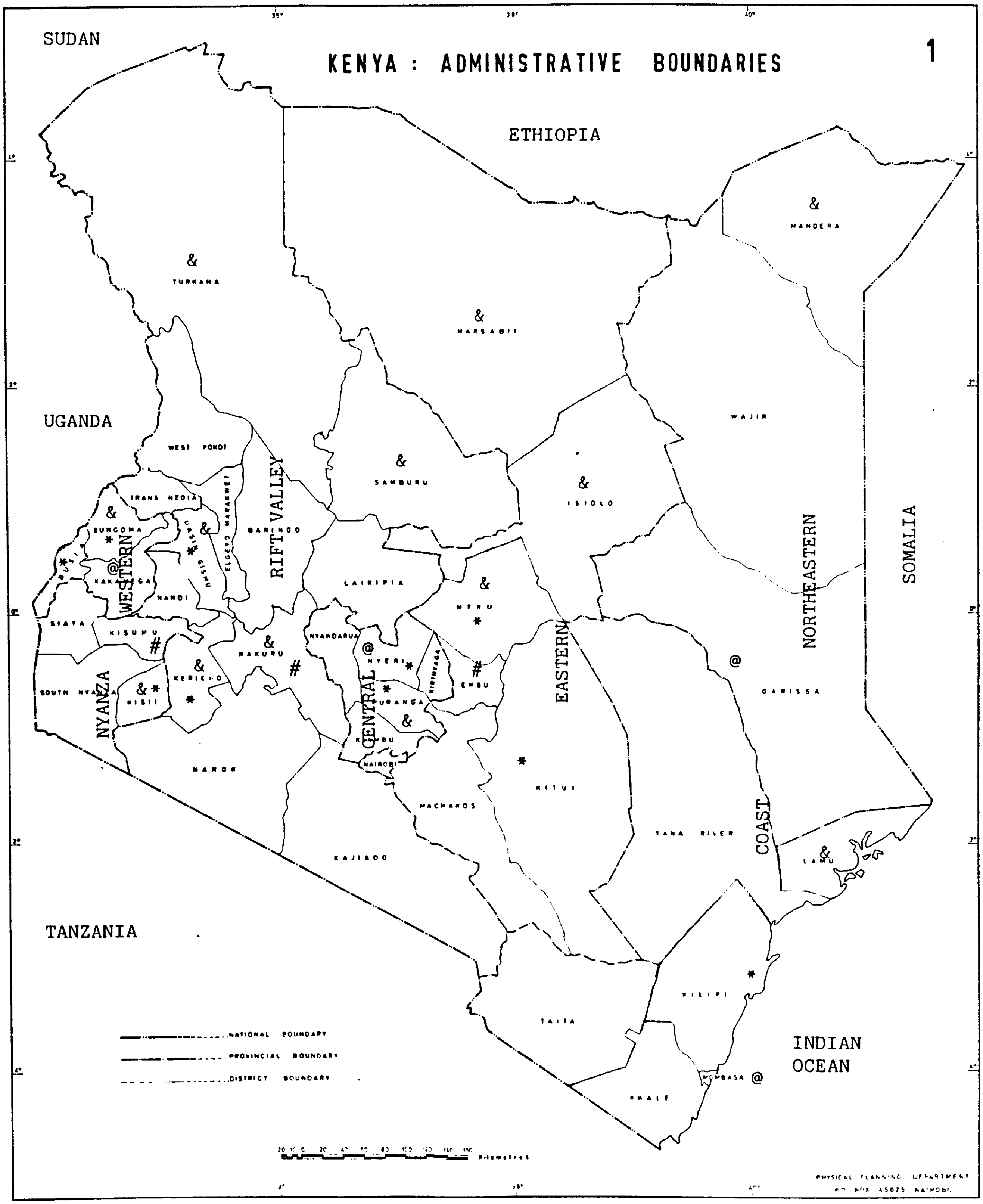
Kisumu	Municipal	Kisumu	Nyanza
Malindi	Municipal	Kilifi	Coast
Meru	Municipal	Meru	Eastern
Muranga	Municipal	Muranga	Central
Nakuru	Municipal	Nakuru	Rift Valley
Busia	Town	Busia	Western
Karatina	Town	Nyeri	Central
Kitui	Town	Kitui	Eastern

PROVINCIAL LOCAL GOVERNMENT OFFICE SITE VISITS

Province	Provincial Capital Town
Central	Nyeri
Coast	Mombasa
Eastern	Embu
Northeastern	Garissa
Nyanza	Kisumu
Rift Valley	Nakuru
Western	Kakamega

The map on the following page shows the provincial and district boundaries in Kenya and the sites of the field visits. On the page after that is a list of the districts in each of the provinces in Kenya.

LOCATIONS OF SITE VISITS



* = municipal or town council in study
& = county council in study
\# = provincial capital and municipal council in study
@ = provincial capital, local authority not in study

LIST OF PROVINCES AND DISTRICTS

CENTRAL PROVINCE

Kiambu
Kirinyaga
Murang'a
Nyandarua
Nyeri

COAST PROVINCE

Kilifi
Kwale
Lamu
Malindi
Mombasa
Taita-Taveta
Tana River

EASTERN PROVINCE

Embu
Isiolo
Kitui
Machakos
Marsabit
Meru

NAIROBI PROVINCE

Nairobi

NORTHEASTERN PROVINCE

Garissa
Mandera
Wajir

NYANZA PROVINCE

Kisii
Kisumu
Siaya
South Nyanza

RIFT VALLEY PROVINCE

Baringo
Elgeyo Marakwet
Kajiado
Kericho
Laikipia
Nakuru
Nandi
Narok
Samburu
Trans Nzoia
Turkana
Uasin Gishu
West Pokot

WESTERN PROVINCE

Bungoma
Busia
Kakamega

APPENDIX II

DEFINITIONS FOR REVENUE AND EXPENDITURE CATEGORIES

A. REVENUE

CESS: tax on agricultural production; also used to refer to local taxes on hides and skins, miraa export and livestock export.

BUSPARK FEES: charges paid by public transport operators for use of the local authority's central bus park; normally a fee paid each time the operator enters the park to pick up passengers.

CONSERVANCY CHARGES: fees paid for conservancy services (trash collection).

GRANTS: all types of grants from the Government of Kenya for current account expenses, including grants to needy councils and teachers salaries grants.

HOUSE RENTS: rents on houses owned by the local authority, tenant purchase revenues, and all other housing revenue.

INTEREST: interest on bank accounts and investment.

MARKET FEES: market entrance fees, livestock auction fees, and stall rents in local authority markets.

NURSERY FEES: nursery school fees only.

PLOT RENTS: rents paid on commercial plots owned by the local authority.

POLL RATE: area poll rate (head tax).

RATES: all types of land rates (taxes): urban site value (unimproved) rate, area rates, and agricultural rates.

SEWERAGE CHARGES: monthly service charges and connection fees.

SLAUGHTER FEES: charges for livestock slaughter and transport from local authority slaughter houses and slabs.

STOCK FEES: livestock auction fees.

TOTAL INCOME: all income from all sources except tourism; only the excess of tourism revenues over tourism expenditures is included.

TOURISM FEES: game reserve entrance fees, lodge rentals, income from hotels and hostels, etc.

VETERINARY FEES: all fees for veterinary (dipping, vaccination, etc.), agricultural, and forestry services.

WATER CHARGES: rural and urban water supply charges, meter rents, and connection fees.

WORKS CHARGES: conservancy, plan fees, construction permits, sanitation charges, vehicle and equipment rentals, etc.

B. EXPENDITURES

ADMINISTRATION: clerk's department, treasurer's department, revenue collection, enforcement, and miscellaneous administrative expenses.

CONSERVANCY: conservancy (trash collection) expenses.

COUNCILLORS: councillors expenses, travel allowances, Mayor's Parlor, miscellaneous items.

ENGINEER: planning, drawing, and valuation.

HOUSING: rental and tenant purchase housing.

LIVESTOCK: stock auction yards.

MARKETS: markets, trading centers and stock auction yards; also sometimes includes bus parks.

NURSERY SCHOOLS: teachers salaries and other nursery school expenses.

PRIMARY EDUCATION: teachers salaries and other school expenses.

PUBLIC HEALTH: hospitals, clinics, and drugs.

SEWERAGE: sewerage expenses only.

SLAUGHTER: slaughterhouses and slaughter slabs only.

SOCIAL SERVICES: social services, nursery schools, special schools, orphanages, sports facilities, youth centers, and parks.

TOTAL EXPENDITURE: total expenditure in all categories except tourism.

TOURISM: game parks, lodges, hotels and hostels.

VETERINARY SERVICES: dipping, vaccinations, drugs, tree nurseries, demonstration shambas, and all other veterinary, agricultural, and forestry services.

WATER: water supply only.

WORKS: buildings, roads, vehicle garages, public conveniences, conservancy, sanitation services, etc.

C. SURPLUS/DEFICIT

SURPLUS/DEFICIT: includes all revenues and expenditures for county councils except tourism revenues and expenditures; for municipal councils includes only general fund finances.

TOTAL SURPLUS/DEFICIT: deficit or surplus including all sources of revenues and expenditures.

NOTE: Some of the income and expenditure categories defined above are aggregates and may include some items that are also listed separately. Disaggregate income and expenditure items may not always add exactly to total revenue and expenditure figures for a given local authority. Some miscellaneous items do not fit well into any of the disaggregate categories, but are included in the total figures.

APPENDIX III

PROBLEMS OF DATA COLLECTION AND ANALYSIS

This appendix discusses some major conceptual and empirical problems with the data analyzed in Chapters 4 to 6 and it explains how some of these problems might affect the results of the analysis. There are a few general problems with the finance data, as well as problems in the estimation of population and wealth, two important variables used in the analysis. Population was used to put income and spending data on a per capita basis, and both population and wealth were used in the regression analysis of total expenditure.

Finance Data

The finance data used in this analysis are not fully complete and compatible for all income and expenditure categories across all local authorities. The most difficult problem in assembling the income and expenditure data was the lack of uniformity in the way local authorities collect and report financial information. Markets, for example, are sometimes in a category of their own, but in some local authorities are reported under the treasurer's department, the clerk's department, the social services' department, or the housing fund. Slaughterhouses are sometimes a separate department, but frequently listed under other departments, such as markets, works, public health, sanitation, or veterinary services. Even services such as water and sewerage do not always have their own departments. They are sometimes reported under works, engineering, or public health.

Another data problem was the wide variation in the level of aggregation of financial data across divisions of local authorities and income and expenditure categories. This is particularly an issue in county councils, where financial data are sometimes reported separately for individual divisions and trading centers. It was usually possible to extract or calculate the required data from these records, but in a few cases, the data for trading centers are classified under broad income and expenditure categories that could not be disaggregated. These are but a few examples of the tremendous variation in the way local authorities keep accounts and records.

Attempts were made to standardize revenue and expenditure categories so that comparisons could be made across local authorities. These categories are defined in the previous appendix (Appendix II). This standardization process involved using disaggregate data to reclassify some types of revenue or expenditure from one category to another. Thus, in some cases, the data used in this research will not closely resemble the summary information presented by local authorities in their official annual budget estimates.

In some cases, it was not possible to disaggregate sources and uses of income data sufficiently to be able to assign consistent and correct numbers to all income and expenditure categories for all local authorities. Some local authorities do not keep records in a way that permit this. Thus, despite every effort to be consistent, there are some unavoidable distortions in the data.

These disaggregation and reporting problems strongly point to the need for the Government of Kenya to provide the Ministry of Local Government with the funds to develop a standardized accounting system for local authorities. This would facilitate the work of both local authorities and the Ministry as well as provide analysts with a reliable database for making cross-council comparisons.

Only one year of data, fiscal year 1984, is formally analyzed in this study.[1] A study covering a longer time period would obviously have been more useful, but there were a number of major obstacles involved in obtaining time-series data. Some local authorities are unable to provide printed copies of budget estimates for even a single year much less several, so that information had to be copied by hand, photocopied, or calculated from other records. It was also sometimes difficult to get information from the treasurer's

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[1] Because of the 1984 drought, that year was not a typical one and is therefore not an ideal choice for the analysis. It is, however, the most recent year for which data are generally available, and using an earlier year would have caused comparability problems because local authorities changed from a calendar fiscal year to the Government of Kenya's fiscal year (July 1 to June 30) at different times during the first few years of the 1980s.

records because they were unavailable, undecipherable, or being used in attempts to produce audited final accounts. Photocopying facilities were often unavailable or difficult to get access to. Another problem is that as local authorities change chief financial officers over time, there are sometimes changes in how records are kept. Finally, in recent years most local authorities have switched from keeping records on a calendar year basis to a Government of Kenya fiscal-year basis, making comparisons across time more difficult.

For all of these reasons, it was decided to focus on an in-depth analysis of one year of financial information for all of the local authorities being studied. The year 1984 was selected because it is the most recent year for which actual (as opposed to budgeted) income and expenditure data were generally available. Some sense of how revenues and expenditures change over time was also obtained from those local authorities for which several years of data were readily available.

It should also be noted that the accounts of some of the local authorities examined in this study have not been properly audited. There is no way of verifying the accuracy of these figures. Nevertheless, these data have been used in the study because they are the only information available.

Population

The population figures used in this analysis have some limitations that should be recognized. The most recent population census in Kenya was conducted in 1979, while the financial data being analyzed are for 1984. The Central Bureau of Statistics of the Ministry of Planning and National Development does provide population projections for districts in years between censuses. Because county councils are in almost every case geographically identical to districts, the district figures were used to estimate county council populations. The 1984 district population projections (assuming constant mortality and fertility) were adjusted downward by subtracting from them the estimated 1984 populations of municipal and town councils located in the district. This was done because county councils are theoretically responsible for service provision in all areas of a district that are not serviced by municipal or town councils, including urban councils.

There are two problems with this definition of county council population. First, the municipal and town council populations that were subtracted from district totals were not available from the Central Bureau of Statistics and had to be roughly estimated, as will be explained below. Second, it is clear that county councils do not provide services or collect revenue uniformly in all areas under the councils' jurisdictions. To analyze the issue of per capita spending or income properly, it would be necessary to know two things: (1) What portion of the county is actually covered by the service or revenue collection?; and, (2) What is the per capita expenditure or income within the relevant population? Needless to say, such information is not available.

Other issues arise in the case of municipal and town councils. Because no population figures for these councils are available from the Central Bureau of Statistics, five methods were used to calculate a set of estimates for 1984. The five results were compared, and it was decided to use the figures based on annual average population growth between the 1969 census and the 1979 census, with certain adjustments made for those councils suspected of having grown faster. This was considered to be about as reasonable an estimate as any given the existing data constraints.

The other problem with municipal and town council population figures is similar to one of those discussed regarding county councils: total population is used in the analysis rather than serviced population. As with county councils, service provision and revenue collection are not uniform within municipal and town councils. Some municipal councils are completely urbanized, while others have substantial rural areas within their boundaries. There are rough estimates available of the breakdown between urban and rural land within municipalities, but using these data might obscure other issues. Some municipal councils do collect revenue and provide services in rural areas of the council, while others do not collect revenue and provide services in some urbanized sections.

Wealth

The measure of wealth used for county councils is a measure of local economic surplus, i.e., a measure of the ability of the county council residents to produce beyond their subsistence needs. It is developed from two sources. The first source is household saving from the Central Bureau of Statistics Household Budget Survey of 1981-82. This survey was conducted largely among small landholders in rural areas of districts, so that the saving figure is used as a measure of surplus for that segment of the population. The Central Bureau of Statistics data are household figures, but were converted to per capita figures using data on persons per household by district from the 1979 population census.

The second type of information used in constructing a measure of wealth for county councils is per capita centrally marketed agricultural and livestock sales, which include output sold through parastatals, marketing boards, and producing companies. This information is used as a rough measure of surplus production by large-scale farmers and ranchers. These sales figures were added to the small-holder per capita saving figures described above to obtain a crude measure of per capita wealth for county councils.

It is possible to argue that property value would be the best way to measure wealth in county councils, including both urban land in the trading centers under the jurisdiction of the council and agricultural land. This information would be very difficult to obtain for several reasons. First, reliable data about rated land in small urban areas and trading centers are not readily available. Second, some areas of urban land where trading activities take place in county councils have been neither formally surveyed nor rated. Third, much agricultural land in county councils is neither rated nor taxed. Agricultural land taxes do exist in some councils, but the tax is often a fixed sum per acre, and there is no easy way to put a value on the land. In some councils that have no tax on agricultural land, there is a tax on agricultural output (cess). However, it is sometimes only on one or a few crops.

For all of these reasons, it was decided to use the measure of economic surplus discussed above as a crude measure of county council wealth. Nevertheless, it must be pointed out that there are a few serious flaws in the data used to construct this measure. First, not all districts were included in the Household Budget Survey from which the small-holder savings figures were taken. Some northern and eastern districts, which are semi-arid and populated largely by nomadic herders, were not covered in the survey. Several of the county councils in this study were among those not included in the survey, so their effective per capita savings figures are zero. It can be argued that zero is an appropriate measure of savings in a formal economic sense. Few of the pastoralists in the semi-arid areas are involved in the formal sector, most are not likely to have much use for significant amounts of Kenyan currency, and a high percentage probably lead a subsistence existence. Nevertheless, there is clearly wealth in the area, primarily in the form of livestock, and it is unsatisfying to have it excluded from the measure of surplus.

Another problem with the measure of county council wealth revolves around the use of centrally marketed agricultural and livestock sales in the calculation of the data. This is probably a reasonable measure of surplus in some cases, but the measure does not fully reflect the value of economic activity in the local agricultural sector in some districts. Furthermore, a significant percentage of centrally marketed agricultural output is produced by small holders in some districts, leading to an element of double-counting in the overall measure of wealth. Perhaps more importantly, the marketing organizations rarely do business in some of the northern and eastern districts. There is little or no agriculture in these semi-arid areas, so the agricultural marketing groups have no occasion to do business here. Livestock-related organizations, such as the Kenya Cooperative Creameries and the Kenya Meat Commission, do not often go to these areas for at least several reasons. First, the costs and distance involved in transporting livestock and milk from the northern districts may seem to be prohibitive. Second, the animals in these dry areas may be (or at least are perceived to be) of an inferior quality--poorly nourished compared to their southern counterparts, and perhaps more likely to be diseased due to a lack of available veterinary care. Third, the main business of the livestock marketing groups is in central and southern Kenya. If they can satisfy their needs for meat and milk locally, they will not be bothered to set off for the distant parts of the country. Meat in the northern districts and many other rural areas is marketed and processed through local auctions, county council slaughterhouses and slaughter slabs, and local butcheries. In more rural areas, people take care of their own requirements.

Despite all of the above objections to the measure of county council wealth used in this study, it was used for lack of a better alternative. Efforts are currently underway in the Ministry of Planning and National Development to construct a better indicator of county council wealth, but the new data will not be ready in time for use in this study.

The measure of wealth used for municipal and town councils differs dramatically from the one used for county councils. The municipal council measure is land value per capita, a very reasonable measure of wealth for urban areas.

Land valuation is a good measure of the level of economic activity in a local authority and will directly affect the demand for public services as well as the ability of a council to raise public revenue. Land taxes, although not as significant as in some western countries, are an important source of revenue for municipal and town councils in Kenya. Furthermore, many local authority taxes are raised from formal sector businesses (business license fees, buspark fees, slaughter fees), and informal sector activities (market fees and hawker fees). Finally, if land values are correlated with economic activity, they will also be related to demand for municipal services such as housing, roads, water, and sewerage, which are important service activities and/or sources of revenue for local authorities, particularly municipal councils.

For all of these reasons, land value per capita is expected to be a good measure of wealth in urban areas. Nevertheless, there are a few problems with using land values as a measure of wealth in municipal councils. First, all urban land is valued on the site only. The value still rises with the level of economic activity, but it is not as good a measure of economic activity as valuation based on improvements. Second, land in Kenya is revalued only every five years, but it is done at different times for different local authorities. Most of the revaluing is done by the Ministry of Lands and Settlement, which is very much behind schedule in its work. Thus, land values in different local authorities were assigned at different times, and there are no measures of equalized valuation. This means that land values are not strictly comparable across all local authorities. Finally, some local authorities have significant areas of commercial and residential land that have not been formally surveyed and valued by the Ministry of Lands and Settlement. This also leads to comparability problems across local authorities.

Despite the data problems outlined in this appendix, the type of analysis provided in this paper is believed to be a step in the right direction in terms of trying to understand variations in patterns of local authority finance and their causes. The problems point to the importance of more extensive and uniform data collection by the Government of Kenya if better analysis of local authority finance and the district-level economy is to be conducted in the future. Possibilities to improve the quality of local authority data are currently being explored by the World Bank and the Ministry of Local Government.

APPENDIX IV

TRADITIONAL URBAN DEVELOPMENT POLICIES VERSUS THE NEW RURAL-URBAN BALANCE STRATEGY IN KENYA

Kenya has followed a fairly consistent urban development policy since independence. In 1986, however, the Government defined a new type of urban development policy. This appendix reviews both the traditional and new policies.

Traditional Urban Development Policies

Traditional urban development policies in Kenya have focused primarily on physical planning. They have involved attempting to establish a hierarchy of urban service centers through strategies designed to coordinate land use by carefully planning the location of investments in physical infrastructure and implementing incentives to affect the location of new industry. These policies were carried out in the context of a set of priorities that included redistribution, a strong emphasis on social services, and an attempt to promote regional balance by shifting the focus away from the largest cities towards the smaller urban areas throughout Kenya.

The planned network of urban centers was designed to provide a hierarchical arrangement of towns and village settlements. The different levels of the hierarchy were supposed to be given different functions and to provide different types of infrastructure commensurate with their role and the size of their service area. The four levels of designated service centers are: Urban Centers, Rural Centers, Market Centers and Local Centers. These centers respectively were to serve catchment areas of 120,000, 40,000, 15,000, and 5,000 people. The 20 municipalities in Kenya are special cases of Urban Centers referred to as principal towns, and generally provide a still higher level of services.

<u>Problems With Traditional Urban Development Policies</u>

Although some advances have been in urban development in Kenya, these traditional urban policies have not had the full expected impact, particularly on the smaller urban centers, for a variety of reasons. First, implementation of these policies required a great deal of local capacity and coordination among many different Government of Kenya ministries. The local capacity was often extremely deficient, and coordination was often difficult to organize, particularly at the level of dealing with the specifics of particular local investments. In addition, these traditional policies looked at the problem of urban development in isolation rather than in the broader context of agricultural and rural development in the hinterland surrounding urban areas. Even though the policies were supposed to strengthen local economies throughout the entire country, they focused essentially on providing infrastructure and encouraging commercial and industrial development in some of the larger secondary urban areas. The Government of Kenya now argues that urban development policy is only one part of a comprehensive development strategy and that it must take account of rural-urban linkages, agricultural productivity, and overall macroeconomic policies and priorities. Finally, a variety of changing circumstances in Kenya required a degree of flexibility and responsiveness that the traditional urban development policies were unable to provide.

Changes in the Kenyan Economy

Several major changes have occurred in Kenya during the past decade. These changes have had an important impact on the nature of the priorities required to be dealt with by Government of Kenya policies. The first of these changes is that the rate of population growth has been on the rise, while the rate of economic growth has generally been slower, partially due to a declining productivity of investment. The government believes that this situation necessitates focusing more on increasing the growth of income rather than on redistributing it. Policies should therefore focus on concentrating scarce resources in areas with high, but unrealized, potential where investments are likely to bring higher yields and create more productive employment opportunities. Urban policies designed to deal with these issues would be consistent with broader macroeconomic goals and explicitly recognize the role of the rural-urban system in the national economy.

A second major change that has occurred in Kenya in recent years has been the rapid growth of public expenditures and the rise in Government deficits. The implication of this development is that Government expenditures cannot continue to expand at their historical rate, and the Government of Kenya must try to focus on self-financing and more productive public investments. This means putting less emphasis on social services, such as health and education, and more on basic infrastructure services, such as water, electricity, and roads. It also requires that a greater emphasis be placed on cost recovery in projects where this is feasible. Finally, it suggests that the central government may have to reduce its role in managing certain policies such as urban development and rely more on local authorities, which are often underutilized and have untapped revenue potential.

The last major change in Kenya's economic situation that impacts on urban policy is the dramatic rise in foreign debt to what might be considered unhealthy levels. This suggests that the Government of Kenya must reduce its dependence on foreign capital and the large-scale projects that this capital is often used to finance. The government plans to use its own scarce resources more productively, and job-creation policies should focus on the informal sector and small-scale enterprises, where employment is much less expensive to create than it is in larger enterprises.

Other Economic and Demographic Factors

In addition to the factors and changes outlined above, several other facts of Kenya's present reality have figured prominently into the design of the new rural-urban balance strategy. The high rate of population growth necessitates that the Government design policies to absorb the expected growth in the labor force during the coming years. Agriculture is and will remain for the foreseeable future the backbone of the Kenyan economy. However, because most of the arable land in the country is currently under cultivation and because of the fear that the largest cities have grown too large, it is expected that the bulk of new jobs will have to be created in the nonagricultural sector in smaller urban centers in the rural areas outside of Nairobi, Mombasa and Kisumu. With only an estimated 15 percent of its total population living in urban areas, Kenya is a highly underurbanized country. However, the growth of urban population is expected to increase at a rate of about seven percent per annum during the next 15 years. The reliance of the national economy on the agricultural sector and the expected increase in urbanization will create a situation that demands a strategy designed to promote a process of interactive rural-urban development.

The Rural-Urban Balance Strategy

The rural-urban balance strategy outlined in Sessional Paper No. 1 of 1986 and currently being implemented by the Ministry of Planning and National Development is being hailed as the beginning of a new generation of urban development policy in Kenya. This strategy explicitly recognizes and deals with the interactive effects between rural and urban areas, the linkages among different sectors of the national economy, and the Government of Kenya's principal growth priorities. It is designed to promote the development of a well-serviced urban system that facilitates the distribution of agricultural production, provides inputs and support services to both the agricultural and nonagricultural sectors, and generates productive nonfarm employment in urban centers and rural areas. The success of this strategy will depend to a great extent on other Government of Kenya strategies aimed at raising agricultural productivity and farm incomes, which will generate increased demand for nonagricultural goods and services produced in the small towns and rural areas.

Objectives

The main objectives of the rural-urban balance strategy, as outlined in Chapter 4 of Sessional Paper No. 1 of 1986, are:

(a) To avoid the excessive concentration of population in

Kenya's largest cities;

(b) To promote the vigorous growth of secondary towns and smaller urban settlements through the development of agriculture;

(c) To foster production linkages between agriculture and other sectors of the economy, between rural areas and local service centers, market towns, gateway towns and secondary cities; and,

(d) To bring renewed economic growth to all regions of the country, so that even the least-developed regions can share in the general growth of the economy.

Rural-Urban Balance Strategy Policies

The Government of Kenya's rural-urban balance strategy focuses on three major policy areas: Rural Trade and Production Centers (RTPCs), strengthening local authorities, and creating informal sector employment. Each of these will be briefly discussed.

<u>Rural Trade and Production Centers</u>

To achieve these objectives in the context of the overall framework outlined above, the Government of Kenya will focus on three principal policy areas. First, it will concentrate scarce resources in designated small towns to be known as Rural Trade and Production Centers (RTPCs). Resources will be used to provide basic infrastructure and services designed to support the growth of agricultural and nonagricultural activities in the urban center and its surrounding hinterland. Thus, the strategy is designed to exploit and strengthen both sectoral and rural-urban linkages. This RTPC effort will be coordinated by the Ministry of Planning and National Development, which will work closely with the District Development Committees in establishing RTPC sites and planning investment packages. Implementation support and funding for these RTPC investment packages will be provided by the District Development Fund, a new section established in the Ministry of Planning and National Development. Many other operating Government ministries will also have an important role to play in RTPC implementation. The RTPC Programme will focus on small urban centers, but the Government will continue to support development projects in larger centers as well.

Strengthening Local Authorities

The second component of the Government's strategy will be to strengthen local authorities to enable them to play a more substantial and effective role in promoting local development than they presently do. As noted earlier, the Government of Kenya will need to rely more heavily on local skills and resources in the coming years than it has in the past.

The Government has been concerned for some time about the effectiveness of its local authorities. They are supposed to play a major role in service provision at the grassroots level but have been plagued by a variety of institutional and operational difficulties, as discussed in the main text. The most significant problems of the local authorities are inadequate sources of revenue, institutional bottlenecks, and poor financial management.

For several years, the Government has recognized these problems and taken some steps towards alleviating them. The Ministry of Local Government (MLG) has instituted the preparation of Local Authority Development Programmes, long-range capital plans that have been developed in a sample of local authorities and will soon be required of all of them. The Government has been investigating additional sources of revenue for local authorities and has already made some proposals in this area. An extensive training programme in financial management for local authority officials has also been set up, and the MLG has developed revised local authority financial regulations. Other important work on strengthening local authorities, including the development of a standardized accounting code for local authorities and reforming MLG procedures for monitoring local authorities, is also planned or underway. Many of these measures, however, are procedural in nature and will not be effective unless more basic institutional problems are corrected. For example, local authority officer training will not have much effect unless centrally-imposed constraints are relaxed, greater accountability is introduced, and a system of effective incentives is implemented.

Pursuant to Sessional Paper No. 1 of 1986, the Government is also working on plans for restructuring the Local Government Loans Authority (LGLA) into a Municipal Development Bank. The LGLA, which is the main source of finance for local authority investment, has had increased demands on its resources because of the rapid growth of local authorities and has experienced some problems that could be alleviated through reorganization.

Given some additional administrative training and revenue-raising and enforcement powers, the Government of Kenya believes that local authorities have the potential to play a major role in the development, operation, maintenance, and expansion of the RTPCs and other local development projects. The strengthening of local authorities will also require a strengthening of the capacity and operating procedures of the Ministry of Local Government and a reorganized Local Government Loans Authority.

Promoting the Informal Sector

The final major component of the rural-urban balance strategy is the implementation of policies to promote the growth of productive nonfarm employment opportunities in the rural centers. As noted earlier, rapid population growth and limits on the expansion of employment in agriculture and formal sector industrial and commercial activities require that the bulk of new employment be generated in small-scale enterprise and informal sector activities. Policies to stimulate this sector would include agricultural pricing policy and support programs that raise farm income, lower tariffs on inputs used by small-scale manufacturers, and an investment incentive structure that encourages the substitution of labor for capital in order to encourage more labor-intensive small-scale activities. In addition, policies aimed at expanding training opportunities, increasing the flow of information, augmenting credit availability, and removing legal constraints on kiosk-operators and hawkers would have the potential to expand employment in the informal sector greatly.

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In conducting the field work in Kenya, 1983-88 District Development Plans, which were produced by the Ministry of

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